Maritime Life

2002 Maritime Life

Annual Report

THE MARITIME LIFE ASSURANCE COMPANY

Service Sets Us Apart

If it's good for the customer and you know it makes sense, then do it.

IN THE FINANCIAL SERVICES industry, financial strength is expected, but service excellence sets you apart.

Customers want quality products, reliable services and flexible options to meet their changing needs. They are finding it at Maritime Life.

From coast to coast, customers identify Maritime Life as a company with a strong service culture. It is something they remember about us, and makes us different from our competition.

Doing what's best for customers, employees and business partners has always been our focus. If it's good for the customer and you know it makes sense, then do it – is a commitment that's well ingrained.

Today, it is driving us to develop better products, faster operating systems and deeper customer relationships. At Maritime Life, customers have come to expect service excellence that is second to none. Delivering on this expectation is what sets us apart.

President's Message

THE YEAR 2002 brought many challenges including market swings and decreased investor confidence. Maritime Life's profits were affected, especially compared to the record results of 2001. Several impacts were one-time items – one example is the cost associated with our integration of Royal & SunAlliance Financial, which will help position us for future growth. When we look at our results and what they tell us about the future, the fundamentals of our business remain strong.

Two of those fundamental strengths are customer and employee satisfaction. We believe they lead to long-term profitability.

According to our annual surveys, customer satisfaction improved last year for group insurance and pension customers – both areas saw customer responses of more than 90 per cent satisfied. On the retail side, customer satisfaction improved for protection customers and stayed about the same for investment product customers, despite lacklustre performance in the equity market. Qualitative market research also tells us that we are identified by Canadians as a company with a service culture that sets us apart from our competition.

Through our annual employee survey, we know 91 per cent of our employees are satisfied overall. We were recognized again by the *Globe and Mail's Report on Business* magazine in "The 50 Best Companies to Work for In Canada" ranking. It's an achievement only three companies have earned in each of the four years the survey has been produced.

Due to the volatile market conditions, many of our competitors experienced sharp drops in their retail investment product sales; however, ours remained steady. Our pension sales grew and the marketplace showed its confidence in Maritime Life's strength by buying $100 million of new preferred shares and $350 million of our new institutional annuities product. Our investments department has rapidly added margin to our acquired assets while maintaining good quality. With the notable exception of a $15 million loss on a Teleglobe Inc. investment, we have had another year of favourable credit experience.

While we recognize our business strengths, it is also important to address significant issues. We need to:

> Qualitative market research tells us that we are identified by Canadians as a company with a service culture that sets us apart from our competition.

1. Better manage expenses. In the past two years, expenses have grown faster than revenue.
2. Deliver systems development projects on budget, faster and ensure the benefits are fully realized.
3. Improve on-line services in the remaining areas where we are not equal to, or ahead of, our competition.
4. Improve visibility amongst our key audiences — particularly executives of medium- and large-sized employers and their advisers.
5. Regain our leadership position in the delivery of individual products and increase our satisfaction levels among distributors.
6. Contact our retail customers more frequently, with reports that are easier to understand.

As the industry continues to consolidate, Maritime Life will rank among the top four Canadian providers in each of our largest business areas: group insurance, retail protection products and life company segregated funds. Along with our three competitors, we'll serve more than 60 per cent of the group insurance market, more than 64 per cent of the retail protection product market and more than 74 per cent of the life company segregated funds market.

This can be a more attractive and disciplined environment compared with the highly fractured and price-competitive landscape of the last decade. But it means that we have to execute our game plan very well.

Clearly acknowledging our challenges is a necessary first step to solving them. The management team has established plans to address each of the issues previously mentioned. Based on our track record of success over the past several years, I know our challenges will be met.

At the same time, we will maintain and enhance those things that have distinguished us from our competitors — excellent customer service, agility, accessibility, flexibility, responsiveness, and a common sense approach to business decisions.

Sincerely,

W.A. Black

William A. Black
President and Chief Executive Officer

Corporate Profile

In 2003, for the fourth consecutive year, the *Globe and Mail's Report on Business* magazine named Maritime Life one of "The 50 Best Companies to Work for in Canada."

MARITIME LIFE is the fourth largest insurance company in Canada, according to 2001 figures for Canadian individual life insurance and group insurance revenue premium. We offer customers from coast to coast a variety of personal insurance, disability and critical illness insurance, investment products, pension and retirement solutions, and group life and health products and services to meet their needs.

For 80 years, we've steadily grown and diversified our product offerings to build and protect the wealth and well being of Canadians. Today, as we always have, we strive to consistently provide excellent customer service and a satisfying work experience for our staff of more than 2,200 employees. Focusing on relationships and service has always been our way.

We are the largest life insurer that sells to individuals exclusively through a national network of independent financial advisors. Through these partnerships, we believe Canadians receive informed advice to meet their particular protection or investment needs.

For large and mid-sized employers, unions and trusteed groups, and professional associations, we offer a broad array of group life, health and disability insurance products. As a provider of pension and retirement solutions, we tailor plans to meet not just the needs of our customers, but their plan members as well.

In 2002, Maritime Life marked a first for the Canadian insurance industry by introducing our institutional annuities program. Under the program, we issue annuities to an independent trust — Maritime Life Canadian Funding – which uses the annuities as collateral for notes it issues to institutional investors.

Headquartered in Halifax, we provide benefits to more than two million customers from offices in Halifax, Montreal, Toronto, Kitchener, Oakville, Calgary and Vancouver. We are an Imagine company and are proud to support our communities through our community investment programs. In 2003, for the fourth consecutive year, the *Globe and Mail's Report on Business* magazine named Maritime Life one of "The 50 Best Companies to Work for in Canada."

For more information, we invite you to visit our Web site at www.maritimelife.ca

Financial Highlights *($ millions)*

Assets Under Administration

2002	14,357
2001	14,116
2000	11,509
1999	10,586
1998	9,097

Capital and Surplus

2002	1,435
2001	1,279
2000	970
1999	889
1998	618

Total Revenue (General Fund only)

2002	2,439
2001	1,881
2000	1,795
1999	1,829
1998	1,610

Net Income to Shareholders (after tax)

2002	62
2001	111
2000	86
1999	36
1998	32

Inforce Individual Insurance Premiums

2002	691
2001	691
2000	542
1999	519
1998	489

Inforce Living Benefits Premiums

2002	92
2001	80
2000	72
1999	67
1998	60

Inforce Group Insurance Premiums and Premium Equivalents

2002	1,650
2001	1,514
2000	1,445
1999	1,330
1998	1,109

Investment Products Assets Under Administration

2002	7,302
2001	7,544
2000	6,136
1999	5,692
1998	4,852

The John Hancock Connection

MARITIME LIFE is a subsidiary of Boston-based John Hancock Financial Services, Inc. and an affiliate of the John Hancock Life Insurance Company. Maritime Life's long-standing partnership with John Hancock has benefited both companies for more than three decades and has enabled each to take full advantage of the other's expertise and operations.

With the life company being founded more than 140 years ago, the Hancock name has long been known for financial strength and stability. The Hancock companies stand by their customers, offering individuals and institutions some of the best products such as annuities, mutual funds, life insurance and long-term care insurance. Today, John Hancock Life is among the highest-rated insurance companies as judged by the major rating agencies. Success is based on the depth of products and outstanding service. John Hancock's vision for the future is one of innovation and a continued focus on customer needs.

As of December 31, 2002, John Hancock and its subsidiaries had total assets under management of US $127.6 billion.

Management's Discussion & Analysis

MANAGEMENT'S Discussion & Analysis (MD&A) presents management's view of the financial position and performance of The Maritime Life Assurance Company ("Maritime Life" or the "Company") for the year ended December 31, 2002 compared with 2001. The MD&A should be read in conjunction with the information disclosed within the annual consolidated financial statements and notes to those consolidated financial statements as determined using Canadian Generally Accepted Accounting Principles ("Canadian GAAP"). The MD&A provides an overall discussion, followed by analyses of the performance of the Company's major reportable segments *(see note 26 to the consolidated financial statements)*. All amounts included in the MD&A are expressed in millions of Canadian dollars, unless otherwise indicated.

Overview

We are a financial services company, providing individual life insurance and living benefits, investment products, pensions, and group life and health products and services. We operate through three major business divisions: the Retail Division, comprised of individual life, disability and investment products, the Pensions & Group Investments Division, comprised of group immediate and deferred annuities and institutional annuities, and the Group Division, comprised of group life, accident and sickness benefits. For segmented reporting purposes, our business segments are now reported as: Retail Protection, Asset Gathering, Group Life & Health and Corporate & Other.

Corporate Organization

On October 1, 2001, we acquired 100% ownership of Royal & Sun Alliance Life Insurance Company of Canada ("RSAF") in exchange for approximately $237 million with the result that RSAF became a wholly-owned subsidiary of Maritime Life. Accordingly, the consolidated financial statements of the Company include the results for RSAF from the date of acquisition. The companies were amalgamated on January 1, 2002 and now operate under the Maritime Life name. RSAF carried on business in similar Retail product lines and so we expect the acquisition will help to financially strengthen and augment our core businesses while providing additional synergy opportunities.

Financial Results in Summary

	2002	2001	
Consolidated net income to shareholders after adjusting for the change in accounting for goodwill amortization	$ 61.8	$ 119.0	(48.1)%
Operating income before income taxes and goodwill amortization — shareholders	113.6	160.8	(29.4)%
Operating income before income taxes — participating account	10.1	30.5	(66.9)%
Shareholders' equity	1,088.1	936.6	16.2%
General fund assets	9,186.9	8,328.6	10.3%
Earnings per common share *(in dollars)*	156.18	293.80	(46.8)%

The Company adopted *CICA Handbook* Section 3062, "Goodwill and other Intangibles", on July 1, 2001. Under that section, goodwill acquired after July 1, 2001 was no longer subject to amortization and goodwill acquired prior to that date ceased to be amortized commencing on January 1, 2002. The table above indicates the comparative result for consolidated net income to shareholders after adjusting 2001 to a comparable basis.

Ratings

	Rating Agency	*Rating*	*Description*
Claims Paying Ability			
	A.M. Best	A+	Superior
	Moody's	A1	Good
	S & P	AA-	Very Strong
	DBRS	IC-2	Satisfactory credit quality
Cumulative preferred shares: (1986 issue – MMF.PR.A)			
	S & P*	A-	Strong
	DBRS	Pfd-2 (high)	Satisfactory credit quality
Non-cumulative preferred shares: (1999 issue – MMF.PR.B)			
	S & P*	A-	Strong
	DBRS	Pfd-2 (high)n	Satisfactory credit quality
Non-cumulative preferred shares: (2002 issue – MMF.PR.C)			
	S & P*	A-	Strong
	DBRS	Pdf-2(high)n	Satisfactory credit quality

** indicates a Global Rating*

Ratings

Our financial and fiscal strength is monitored by external ratings agencies. Favourable ratings give comfort to our policyholders, customers and investors that the Company is prudently managed and financially strong.

Net Income *($ millions)*

Profitability

This year's challenging market environment has impacted current year's results in several ways – falling segregated fund asset values, lower insurance product new sales and asset credit losses. Transitioning our RSAF acquisition and launching our new institutional annuities business also impacted 2002 results negatively but we expect them to make a positive contribution going forward.

Excluding the impact of income taxes and goodwill amortization, income is allocable to shareholders and participating policyholders as follows:

	2002	2001	
Shareholders	$ 113.6	$ 160.8	(29.4)%
Participating policyholders	10.1	30.5	(66.9)%
Income before income taxes and goodwill amortization	$ 123.7	$ 191.3	(35.3)%

Shareholders' income before income taxes and goodwill amortization was down $47.2 million or 29.4%, from the excellent result last year. The business lines contributed $65.7 million to the shareholder pre-tax income result in 2002 compared to $121.4 million in 2001. The Corporate & Other segment accounted for the remainder, including $9.6 million of lower integration and transition costs than in 2001.

The variance in results relates to four major items: credit losses of $18.3 million compared to credit recoveries of $5.9 million in 2001; lower segregated fund fee margins of $8.0 million driven by the impact of declining markets on asset levels (providing less variable fee revenue with which to recover fixed operating costs); lower net changes in actuarial assumptions of $13.9 million (being a net release of $63.3 million in 2002 compared to a net release of $77.2 million in 2001); and a $7.8 million loss from a temporary pricing decision on our Critical Needs products following a change in reinsurance terms.

Income before income taxes allocable to participating policyholders fell by 66.9% or $20.4 million, $12.8 million of which is attributable to lower net changes in actuarial assumptions. Dividends paid to participating policyholders increased $6.3 million, reflecting a full year of RSAF participating business.

Income tax expense for the year reflects a higher effective tax rate of 46.0%, compared to 30.4% in 2001. The 2001 rate was unusually low because of a one-time adjustment to recognize a reduction in substantively enacted future tax rates. In addition, the 2002 rate was increased by nondeductible investment losses incurred during the year.

Sales and Growth

		2002		2001	
Annualized premium from individual and group insurance sales, including rate increases and extensions	$	311.7	$	273.5	14.0%
General fund deposits including group pensions		277.3		228.3	21.5%
Institutional annuities		350.0		—	n/a
Segregated fund deposits		591.2		648.5	(8.8)%

For sales results by segment, see "*Segmented Information*" below. Generally, insurance sales were mixed with good results for our group products and disappointing results for individual insurance compared to 2001. New deposits in 2002 reflect investor interest in guaranteed products. Segregated fund deposits fell as investors shied away from equity market volatility.

Segmented Information

Our reporting segments include Retail Protection, Asset Gathering, Group Life & Health and Corporate & Other. Results by segment are shown in note 26 to the consolidated financial statements. The comments below focus on profitability and growth measures.

Retail Protection

Pre-tax operating income was $20.5 million for the year, down $81.8 million from the strong result in 2001. The decrease included $61.4 million in the non-participating business and $20.4 million in the participating business.

Our non-participating business had pre-tax operating profit of $10.4 million including $12.2 million of favourable changes in actuarial assumptions, offset by a $7.8 million loss resulting from a temporary pricing decision for our

critical illness products following a change in reinsurance terms, as well as losses in the early part of the year from unprofitable RSAF products now discontinued. In 2001, experience factors contributed $18.7 million to pre-tax operating profit and changes in actuarial assumptions contributed a further $53.0 million.

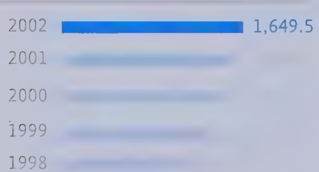
The participating business had $7.9 million contributed from experience in 2002 compared to $15.6 million in 2001, mainly due to increased dividends paid to policyholders as RSAF dividends impacted the full year. Changes in actuarial assumptions contributed $2.1 million to the participating business in 2002, compared to $14.9 million in 2001.

Individual life insurance sales were down 11.6% compared to the result in 2001. Term sales are strong, up 21.9% over last year, offset by universal life sales, which were 8.1% lower than last year. We recently launched a new universal life product that integrates our existing three products into one to simplify our product offerings for customers and make it easier for our distributors to do business with us.

Living Benefits sales continued their strong growth, 35.0% above 2001 premium. Our disability income sales contributed 2.3% growth. Critical illness product sales increased 98.7%.

In the fourth quarter of 2002, individual investment product sales recovered slightly from the lack of confidence in the stock markets. For the full year, new deposits of segregated fund and guaranteed (fixed income) products in aggregate are equal to last year's result. Sales of guaranteed annuity products, excluding the institutional annuities, increased 59.2% from the level in 2001 as investors generally switched from equity market investments to guaranteed instruments. Group pension deposits ended 4.9% behind the 2001 result however sales activity was good in the fourth quarter with premium receipts expected in 2003.

Inforce Group Insurance Premiums and Premium Equivalents *($ millions)*



Asset Gathering

Pre-tax operating income was $32.0 million, up $11.7 million from 2001. Changes in the provisions for future policy benefits contributed $24.4 million to this variance offset by credit losses in the institutional annuities business of $4.3 million and lower segregated fund margins of $8.0 million.

Group Life & Health

Pre-tax operating income was $23.3 million, down $6.8 million from the result last year. Higher operating expenses of $4.8 million and losses of $4.5 million from uncollectible receivables were partially offset by changes in the assumptions for calculating provisions for future policy benefits of $2.5 million.

Subsequent to the year-end, the Company recaptured significant portions of its group life, acciden-

tal death & dismemberment and long-term disability reinsurance. This change in retention, consistent with growth in the Company's capital, will moderately impact the risk profile of this business and result in a corresponding increase in profits.

New sales including policy rate increases and extensions are 21.0% ahead of last year's result, 9.3% for new sales alone. Favourable pricing was the main contributor to the growth in sales.

Corporate & Other

Pre-tax operating income before unusual items was $57.2 million, down $0.9 million from last year. Increased earnings on assets supporting capital and surplus of $8.2 million, $12.5 million lower operating expenses reported in this segment, $2.8 million of interest received on an income tax refund and $2.1 million of additional miscellaneous income was offset by credit losses of $14.0 million, compared to credit recoveries in 2001 of $5.9 million and increased interest on subordinated debt of $4.8 million resulting from the incremental debt used for financing the RSAF acquisition.

Operations

Years ended December 31, 2002 and 2001

Premium revenue was $1,887.3 million in 2002, up 39.2% from $1,356.0 million in 2001. The 2002 result includes $92.2 million of RSAF premium compared to $30.7 million from RSAF from the date of acquisition in 2001. Excluding the impact of RSAF, this represents a 6.9% increase in premium revenue relating to insurance products, and 337.7% for annuity deposits. The annuity deposit increase reflects the impact of the $350.0 million of institutional annuities. Annuity premium growth excluding institutional annuities was 32.0% year over year, driven by higher new deposits for guaranteed products.

Net investment income was $398.9 million, up 1.9% from 2001. This result reflects swings in the volatile market environment for equities in 2002 with some market recovery in 4th quarter of 2002. The positive credit environment experienced in 2001 generally continued in Canada in 2002 with the exception of a $15.0 million write-off related to Teleglobe Inc. bonds. The U.S. environment remained quite volatile, resulting in energy sector credit losses of $4.3 million in our institutional annuities business.

Segregated fund fee revenue grew by $12.6 million, or 12.7% over the level earned in 2001. RSAF contributed $23.6 million to this result in 2002 compared to a contribution of $6.5 million in fourth quarter of 2001. Excluding RSAF, segregated fund fees declined by 4.8% year over year caused by market performance.

Other income increased by $6.9 million, $3.5 million due to higher administrative service only fees. Interest received in 2002 of $2.8 million from a one-time income tax refund is also reflected in this line.

Policyholder benefits paid were up $161.8 million, or 15.5%, in aggregate from 2001. RSAF benefits were not in the 2001 results for a full year and accounted for $52.0 million of this increase. Excluding RSAF, benefits paid increased 10.8% over 2001, consistent with 9.0% premium growth excluding RSAF and institutional annuity deposits.

Changes in the provision for future policy benefits of $666.1

million were up $514.8 million over the change in provision from 2001. Excluding the impact from RSAF and the institutional annuities, provisions for future policy benefits increased by $121.0 million, reflecting higher premium deposits from good sales results for guaranteed annuity products and very good persistency for our individual insurance products.

Commissions and operating expenses, including premium and investment income taxes, were $453.4 million in 2002, up $34.7 million or 8.3% from the level in 2001. Commissions paid were 4.0% lower than in 2001 mainly due to lower insurance sales. Operating expenses were 10.3% higher than 2001 primarily due to increased compensation costs resulting from the addition of the RSAF business for a full year, and higher non-capitalized technology costs.

Interest on subordinated debt was $19.9 million for the year, compared to $15.0 million for the same period in 2001. The RSAF acquisition was financed by the issue of an additional $100.0 million of subordinated debt bearing a fixed weighted average interest rate of 6.9% per annum and $95.0 million of capital from our parent company.

Unusual items for the year include $9.4 million of costs to transition the products, people and processes resulting from our acquisition of RSAF. These activities are now complete. The comparative period included $1.1 million of RSAF transition costs, $1.7 million of cost from vacating surplus office space and $16.2 million of integration costs associated with the Aetna Canada acquisition. The Aetna integration was completed by the end of 2001.

Income tax expense for the year was $56.9 million compared to $58.1 million in 2001, driven by the higher effective tax rate of 46.0%, compared to 30.5% in 2001, on lower pre-tax income as discussed previously.

Quarterly Results

The acquisition of RSAF on October 1, 2001, contributed $56.4 million and $6.4 million to the higher revenue and net income respectively in the fourth quarter of 2001.

Revenue in the first quarter of 2002 reflects the issuance of two institutional annuities totaling $350.0 million in aggregate. Higher revenue in the third and fourth quarters of 2002 represents some modest recovery of stock markets.

Quarterly Results *(unaudited, in millions $)*

	2001				2002			
	1Q	*2Q*	*3Q*	*4Q*	*1Q*	*2Q*	*3Q*	*4Q*
Revenue	$ 416.1	$ 464.4	$ 434.0	$ 566.2	$ 901.9	$ 463.7	$ 488.3	$ 584.9
Net income to shareholders	25.8	13.7	12.0	59.0	27.2	0.5	17.9	16.2
Earnings per common share	67.91	33.49	28.94	163.45	72.62	(3.78)	46.06	41.27

Financial Position

The General Fund assets of the Company exceeded $9.1 billion, up 10.3% from 2001.

Our current asset mix is depicted in the pie chart to the right. Our investment risk is mitigated through diversification of asset type, geographical locale and industry sector. Major groups of in-vestments in our general fund are:

- ***Canada Mortgage and Housing Corporation (CMHC) government-insured mortgages***
  (**12.4%**; 2001 – 12.3%)
  — cover multi-residential developments in cooperation with the Government of Canada and private developers, providing housing to Canadians across the country.

- ***Government bonds***
  (**18.9%**; 2001 – 22.1%)
  — represent obligations of federal and provincial entities across Canada. Government bonds have excellent credit ratings and are highly liquid. The combination of government-insured mortgages and govern ment bonds means over 31.3% of assets are backed by the strength of the federal and provincial governments of Canada.

- ***Private placement bonds***
  (**12.3%**; 2001 – 11.2%)
  — represent investments throughout the North American economy. The portfolio is diversified by industry sector including power generation, manufacturing, transportation and retail holdings in order to reduce risk. These types of bonds are typically funded by a small group of institutional investors and are not widely bought and sold, as is the case for publicly traded bonds.

- ***Conventional mortgages***
  (**13.2%**; 2001- 13.1%)
  — provide financing for real estate in office buildings, retail outlets, warehouse operations and multi-residential developments.

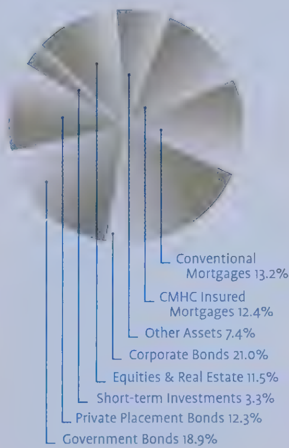
- ***Corporate bonds***
  (**21.0%**; 2001 – 18.7%)
  — are publicly traded and provide good diversity and liquidity.

- ***Equities and real estate***
  (**11.5%**; 2001 – 12.7%)
  — include "own use" real estate,
  a few equity real estate investments, preferred and common stock, both publicly-traded and private, mutual funds and unit trusts like i60's and SPDRs, which are managed to track the S&P/TSE 60 index and S&P 500 index, respectively. More than half of the equities match equity-related investment options that are available to some of our universal life policyholders. These equity investments provide tax efficient diversity for both our policyholders and for corporate purposes.

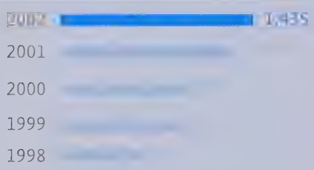
- ***Short-term investments***
  (**3.3%**; 2001 – 1.5%)
  — provide operational liquidity.

General Fund Asset Mix

December 31, 2002



Capital and Surplus *($ millions)*



Invested assets represent 92.6% of the total assets; non-invested assets such as premiums receivable, policy loans and goodwill account for the remaining $678.4 million.

Cash Flow

Cash and cash equivalents increased $132.2 million during 2002, compared to a decrease of $92.5 million in 2001.

Operating cash flow was $503.4 million more than the result in 2001. Investing activities, before capital expenditures and acquisitions used $181.1 million more cash than in 2001, primarily for portfolio re-balancing activities. Therefore, combined operating and investing activities contributed $42.4 million of cash in 2002 compared to a use of cash of $279.9 million in 2001, driven primarily by the RSAF acquisition. Capital expenditures, including capital assets, leasehold improvements, capitalized software and intangible assets, were $26.4 million in the current year, down $3.1 million from 2001 as expenditures on system integration and new systems development were completed.

An opportunity arose during 2002 to issue additional non-cumulative fixed preferred shares and we sold $100.0 million of Series 3 Second Preferred Shares. This capital injection bolstered general cash resources and qualifies as Tier 1 capital for statutory purposes. In 2001, additional subordinated indebtedness of $100.0 million was issued to our parent company, as well as a capital contribution of $95.0 million, to contribute to the financing of the RSAF acquisition. Existing cash resources were used to pay the remaining portion of the purchase price.

The Company intends, when appropriate, to pay common share dividend payments from surplus cash to its immediate parent company as part of its overall capital strategy.

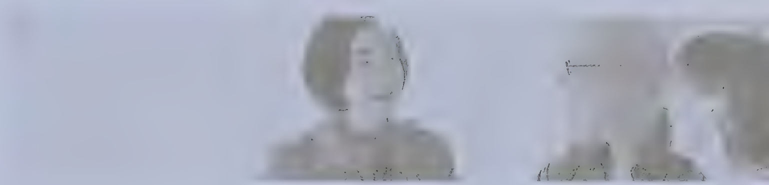
Capital And Liquidity

Total shareholders' equity was $1,088.1 million, up 16.1% from 2001 after our recent Second Preferred Share, Series 3 issue of $100.0 million. Our capital structure reflects a mix of forms of capital available to financial institutions, optimizing our cost of capital while providing security to our policyholders.

The Company's consolidated risk based capital ratio, defined by the Office of the Superintendent of Financial Institutions (OSFI) as Minimum Continuing Capital and Surplus Requirements (MCCSR) was 192% at December 31, 2002 (2001 – 177%). OSFI's definition of eligible capital reflects various forms of capital and surplus. The Company's recent issue of additional non-cumulative preferred shares had a favourable impact on the level of eligible capital.

It is important that any financial institution has access to cash to make policy benefit and expense payments as they come due. Sources of liquidity include readily marketable assets such as government bonds, public bonds, and preferred shares as well as cash and lines of credit. The risk of illiquidity increases if principal and interest cash flows related to assets, liabilities and off-balance sheet items are mismatched. The Company has established a strategic liquidity plan for maintaining a

sufficient level for short-term and long-term highly marketable securities to meet unexpected and adverse business conditions. Operating liquidity is maintained by ensuring an adequate cash flow is obtained from the Company's sources of funding — its premium and investment income, an operating cash float and bank overdraft facilities.



To monitor ongoing compliance with the strategic liquidity plan, the Company uses a strategic liquidity measure. Liability factors range from 100% of the liability if an immediate book value cash out privilege exists to 0% of the liability if there is no cash value (e.g. immediate annuities or term insurance) and an intermediate factor for a liability with a meaningful cash out restriction (e.g. surrender charge or market value adjustment). Similarly, asset factors range from 100% of the asset value of readily marketable assets that have limited price volatility (e.g. government bonds, public bonds and preferred shares) to 0% if the marketability of the assets is considered limited or very time-consuming (e.g. conventional mortgages and real estate) and an intermediate factor for other asset classes (e.g. private bonds, insured mortgages and common stocks).

Upon review of the Company's liquidity risk management policies during 2002 prompted by the introduction of the institutional annuities business, management recommended an increase in the minimum target strategic liquidity ratio to reflect a level more in line with that used by companies having an external credit rating of AA. The Board of Directors has approved this recommendation.

Strategic Liquidity

The principal lever for maintaining an acceptable ratio is adjustment to asset mix. The table below shows the strategic liquidity at December 31:

(in millions of dollars exception ratios)	2002	2001
Total assets	$ 9,187	$ 8,329
Net liquid assets	5,367	4,893
Total policyholder liabilities	7,236	6,630
Net liquid liabilities	1,400	1,357
Strategic liquidity ratio	383%	361%
Minimum target ratio	250%	180%

Risk Management

The Company faces a variety of risks in conducting its businesses. Management has developed policies and procedures to enable it to respond to these risks. The Board of Directors approves the Company's overall risk management policies including policy retention limits and reinsurance limits and receives annually a Dynamic Capital Adequacy Report prepared by the Appointed Actuary which provides guidance to the Board on the significant risks to which the Company may be exposed. Policies relating to product design and pricing are approved by the Chief Actuary & Risk Officer, the Chief Financial Officer and the Chief Executive Officer. The Customer Issues Committee reviews policy marketing strategies, market conduct and customer satisfaction levels and approves the dividend scale for participating policyholders. The Investment Committee reviews policies covering the investment risks, including asset mix, credit risk, interest rate risk, asset/liability matching and liquidity risk. The Audit Committee reviews overall internal controls as well as general and commercial insurance coverage. The Human Resources Committee reviews all staffing and compensation policies and succession plans. The Conduct Review and Corporate Governance Committee reviews the regulatory and risk management compliance processes used by the Company.

Compliance with policies is monitored at defined intervals by the Company's Chief Compliance Officer and internal and external auditors, and is reviewed periodically by OSFI. For additional information on risks and our risk manage-ment practices, reference is made to Notes 7, 9, 10, and 24 in the consolidated financial statements.

Pricing Risk

Pricing involves estimates and assumptions of such factors as mortality, morbidity, future investment yields, expenses and surrenders. Pricing risk is the risk that actual experience will not develop as estimated in pricing. Management of pricing risk includes careful product design, extensive use of modeling and sensitivity testing as well as monitoring through experience studies.

For new Retail products the Chief Actuary & Risk Officer and the Chief Financial Officer review the actuarial assumptions, design and methodology. The Senior Vice President, Retail Marketing reviews the marketing opportunity and sales outlook for new products and the administration capacity and the Chief Investment Officer reviews the investment aspects. The Chief Executive Officer provides the final approval for the product introduction. Profit emergence is compared against pricing assumptions periodically and remedial action can include redesign, re-pricing of new and future policies or adjustment to asset/liability matching strategies. Risk management for new products in the Group Division focuses on review of actual experience against inter-company studies. Pricing of new and renewal business is adjusted according to emerging trends.

Claims Risk

Claims risk is the risk that actual mortality and morbidity experience exceeds underwriting expectations. The Company manages its claims risk through comprehensive underwriting and claims payment guidelines.

Reinsurance is used to mitigate excessive exposure to individual lives or benefits. The Company's maximum retentions, established separately for individual life, living benefits, group life and group health are subject to Board approval. In 2002, the Board approved a revision to these maximum limits to reflect the Company's capacity to participate in a higher level of risk retention given its increased capital base, current financial strength and stability.

Product Performance Guarantees

The Company guarantees minimum rates of return with respect to the savings elements of adjustable and universal life insurance policies. For segregated funds, the Company also guarantees minimum proceeds on the maturity date of a policy or the earlier death of the annuitant.

Risk management for product guarantees includes revision of product features for future new issues, and adjustments to policy charges on existing policies where contract terms allow. For segregated funds' guarantees, the product design and marketing focus have produced a widely dispersed maturity date profile that provides diversification and risk mitigation. The Company regularly monitors its exposure to these guarantees, measures their costs and risk under a wide range of scenarios and reports quarterly to the Investment Committee of the Board.

Interest Rate Risk

The Company's financial position may be affected by its exposure to interest rate risk. Interest rate risk is the risk of economic losses or gains arising from the reinvestment or disinvestments (sale) of assets. If the cash flow from assets supporting the policy liabilities do not match the timing and amount of the policy cash flows, interest rate losses or gains may occur due to changing interest rates in the future. The Company has an asset/liability management program that seeks to achieve an

effective match. The quality of the asset/liability matching program is reviewed quarterly using duration measures and cash flow testing under alternative economic scenarios. This program is also reported quarterly to the Investment Committee of the Board.

Credit Risk

Credit risk is the exposure to loss in the event of non-performance or failure of an investment. Exposure to credit loss is managed through compliance with investment policy standards for quality ratings, maximum single issuer guidelines, diversification of type and location of properties and, for mortgages and real estate, independent borrower and appraisal reviews. Compliance is measured frequently and reported to the Investment Committee quarterly.

Market Risk

Market risk is the exposure to investment loss from general economic and stock market fluctuations. The Company's asset mix guidelines identify limits on the amount and quality of equity investments. Compliance with these limits is reviewed frequently and reported to the Investment Committee quarterly.

Derivative Instruments

The Company uses derivative financial instruments where appropriate to achieve its asset/ liability management strategies and to assist in the management of financial risk, including interest rate and foreign exchange risks. All of the Company's derivative financial instruments are held for hedging purposes, not for speculation. Financial institution counterparties for the Company's derivative activities are rated AA(L) or better by independent rating agencies.

Liquidity Risk

See "Capital and Liquidity"

Other Operational Risks

The Company is exposed to other operational risks including legal, regulatory, human resource, tax, technology, outsourcing and market conduct risks. Senior management develops risk identification and monitoring procedures to manage these risks. Operating management is responsible for implementing these procedures. Internal auditors review the effectiveness of the internal controls and report quarterly to the Chief Executive Officer and the Audit Committee.

Responsibility for Financial Reporting

Management

THE ACCOMPANYING consolidated financial statements have been prepared by management in accordance with Canadian generally accepted accounting principles. When alternative accounting methods exist, management has chosen those it deems most appropriate in the circumstances. The consolidated financial statements necessarily include amounts that are based on management's best estimates and judgment. These consolidated financial statements fairly reflect the financial position and results of operations of the Company within reasonable limits of materiality.

In carrying out its responsibilities, management maintains appropriate systems of internal and administrative controls, consistent with reasonable cost, designed to ensure that the financial information produced is relevant and reliable and that the Company's assets are appropriately accounted for and adequately safeguarded.

Board of Directors

As required by the *Insurance Companies Act*, the consolidated financial statements were approved by the Board of Directors which has overall responsibility for their content.

Audit Committee

The Board of Directors is assisted in its responsibility by its Audit Committee, which consists entirely of Directors not involved in the daily operations of the Company, the majority of whom are not affiliated with the Company. The function of the Audit Committee is to:

- review the annual consolidated financial statements of the Company before they are approved by the Board of Directors; require the management of the Company to implement and maintain appropriate internal control procedures; review such investments and transactions that could adversely affect the well-being of the Company as the External Auditor, Internal Auditor or any officer of the Company may bring to the attention of the Committee;
- meet with the External Auditor to discuss the annual consolidated financial statements and transactions as required;
- meet with the Appointed Actuary of the Company to discuss the parts of the Annual Statement prepared by the Appointed Actuary;
- meet with the Internal Auditor of the Company and with management of the Company to discuss the effectiveness of the internal control procedures established for the Company;

- report to the Board of Directors on the review of the annual consolidated financial statements before approval of the Board of Directors is given.

In carrying out this function, the Committee meets with management to review the decisions made in preparing the financial statements and meets with both the Company's external and internal auditors to approve the scope and timing of the respective audits, to review their findings, and to satisfy itself that the audit responsibilities have been properly discharged.

The Appointed Actuary

- is appointed by the Board of Directors.
- is responsible for ensuring that the assumptions and methods used in the valuation of policy liabilities are in accordance with accepted actuarial practice, applicable legislation and associated regulations or directives.
- is required to provide an opinion regarding the appropriateness of the policy liabilities as at the consolidated balance sheet date to meet all policyholder obligations of the Company. Examination of supporting data for accuracy and completeness and analysis of Company assets for their ability to support the amount of policy liabilities are important elements of the work required to form this opinion.
- is required each year to analyze the financial condition of the Company and prepare a report for the Board of Directors. The analysis tests the capital adequacy of the Company for the ensuing five years under adverse economic and business conditions.

External Auditors

KPMG LLP have been appointed external auditors pursuant to Section 337 of the *Insurance Companies Act* to report to the policyholders, shareholders and to the Office of the Superintendent of Financial Institutions Canada regarding the fairness of presentation of the Company's financial position and results of operations as shown in the annual consolidated financial statements. Their report appears with these consolidated financial statements.

W.A. Black

William A. Black
President and
Chief Executive Officer

Philip J. Pothier
Senior Vice President
and Chief Financial Officer

Auditors' Report

TO THE POLICYHOLDERS AND SHAREHOLDERS OF THE MARITIME LIFE ASSURANCE COMPANY

We have audited the consolidated balance sheets of The Maritime Life Assurance Company and the segregated funds consolidated statement of net assets as at December 31, 2002 and 2001 and the consolidated statements of income, retained earnings, participating account, cash flows and changes in segregated fund assets for the years then ended. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the Company as at December 31, 2002 and 2001 and the results of its operations and its cash flows for the years then ended in accordance with Canadian generally accepted accounting principles including the accounting requirements of the Superintendent of Financial Institutions Canada.

KPMG LLP

Chartered Accountants
Halifax, Canada
January 17, 2003

Appointed Actuary's Report

TO THE POLICYHOLDERS AND SHAREHOLDERS OF THE MARITIME LIFE ASSURANCE COMPANY

I have valued the policy liabilities of The Maritime Life Assurance Company for its consolidated balance sheets at December 31, 2002 and 2001 and their change in the consolidated statements of income for the years then ended in accordance with accepted actuarial practice, including selection of appropriate assumptions and methods.

In my opinion, the amounts of the policy liabilities make appropriate provision for all policyholder obligations and the consolidated financial statements fairly present the results of the valuations.

Byron Corner

Byron Corner
Fellow, Canadian Institute of Actuaries
Halifax, Canada
January 17, 2003

Consolidated Balance Sheets

as at December 31, 2002 and 2001 (in thousands of Canadian dollars)

	2002	2001
ASSETS		
Invested assets *(notes 4, 5, 7 and 8)*		
Bonds	$ 4,788,965	$ 4,330,646
Government insured mortgages	1,142,511	1,027,880
Conventional mortgages	1,211,223	1,087,564
Equities	919,859	935,201
Real estate	140,995	127,072
Short-term investments	304,890	120,097
	8,508,443	7,628,460
Other assets		
Premiums receivable	58,123	72,962
Policy loans	110,557	112,261
Accrued investment income	60,782	54,727
Goodwill, net *(note 3)*	234,042	234,042
Other *(note 6)*	214,931	226,110
	678,435	700,102
	$ 9,186,878	$ 8,328,562
Segregated fund assets under management	$ 5,170,071	$ 5,787,578
LIABILITIES, PARTICIPATING ACCOUNT AND SHAREHOLDERS' EQUITY		
Policy liabilities *(notes 9 and 10)*		
Provision for future policy benefits	$ 6,680,793	$ 6,009,214
Provision for experience rating refunds	121,556	86,878
Provision for policyholders' dividends	28,489	26,251
Policyholders' funds on deposit	242,569	326,619
Benefits payable and provision for unreported claims	68,560	89,018
Notes payable to reinsurers *(note 11)*	94,112	91,935
	7,236,079	6,629,915
Future income taxes *(note 20)*	132,106	131,560
Deferred net gains *(note 12)*	49,182	35,717
Other liabilities *(note 13)*	334,343	252,666
	7,751,710	7,049,858
Subordinated debt *(note 14)*	276,000	276,000
Participating account *(note 15)*	71,056	66,078
Shareholders' equity:		
Share capital *(note 16)*	282,647	185,851
Contributed surplus	536,203	536,203
Retained earnings	269,262	214,572
Total shareholders' equity	1,088,112	936,626
	$ 9,186,878	$ 8,328,562

Contingent liabilities and commitments — *see notes 24 and 25*

See accompanying notes to financial statements

On behalf of the Board:

J D Crawford

W.A. Black

J. D. Crawford
Chairman of the Board

William A. Black
President and Chief Executive Officer

Consolidated Statements of Income

Years ended December 31, 2002 and 2001 (in thousands of Canadian dollars)

	2002	2001
Revenue		
Premiums *(note 10)*		
Insurance	$ 1,381,863	$ 1,236,903
Annuities *(note 17)*	505,416	119,087
Investment income *(note 18)*	398,913	391,556
Segregated fund fees	111,762	99,133
Other income	40,894	33,976
	2,438,848	1,880,655
Policy benefits and expenses		
Policy benefits *(note 10)*	1,201,573	1,039,807
Provision for future policy benefits *(note 9)*	666,132	151,343
Transfer to (from) segregated funds	(68,738)	17,696
Commissions and operating expenses *(note 10)*	403,010	372,196
Dividends to policyholders	25,287	18,328
Premium and investment income taxes	50,417	46,538
Interest on notes payable *(note 11)*	8,210	9,435
Interest on subordinated debt *(note 14)*	19,874	15,027
	2,305,765	1,670,370
Operating income before the undernoted	133,083	210,285
Unusual items *(note 19)*	9,379	19,003
Income before income taxes and goodwill amortization	123,704	191,282
Income taxes *(note 20)*	56,888	58,123
Income before goodwill amortization	66,816	133,159
Goodwill amortization *(note 3)*	–	8,535
Undistributed participating policyholders' income	4,978	14,122
Net income to shareholders *(note 21)*	$ 61,838	$ 110,502

Earnings per common share *(note 22)*

See accompanying notes to financial statements

Consolidated Statements of Retained Earnings

Years ended December 31, 2002 and 2001 (in thousands of Canadian dollars)

	2002	2001
Balance, beginning of year	$ 214,572	$ 111,690
Net income to shareholders	61,838	110,502
Dividends to shareholders:		
Preferred	(7,148)	(7,620)
Balance, end of year	$ 269,262	$ 214,572

See accompanying notes to financial statements

Consolidated Statements of Participating Account

Years ended December 31, 2002 and 2001 (in thousands of Canadian dollars)

	2002	2001
Balance, beginning of year	$ 66,078	$ 54,876
Undistributed participating policyholders' income	4,978	14,122
Acquisition of subsidiary *(note 3)*	–	(2,920)
Balance, end of year	$ 71,056	$ 66,078

See accompanying notes to financial statements

Consolidated Statements of Cash Flows

Years ended December 31, 2002 and 2001 (in thousands of Canadian dollars)

	2002	2001
CASH FLOWS FROM OPERATING ACTIVITIES		
Net income to shareholders	$ 61,838	$ 110,502
Items not involving cash:		
Realized investment losses, net	19,566	15,428
Amortization of deferred, realized and unrealized capital gains	68,101	15,792
Amortization of premiums and discounts	(59,609)	(41,714)
Amortization and depreciation	15,379	16,183
Net provisions and write-offs for (recoveries of) impaired invested assets	18,250	(3,969)
Interest capitalized on invested assets	(8,946)	(7,053)
Interest credited to policyholders' funds on deposit	14,022	18,340
Future income taxes	546	45,977
Increase in policy liabilities	592,142	156,860
Increase (decrease) in premiums receivable	14,839	(341)
(Increase) decrease in accrued investment income	(6,055)	9,858
Decrease in other, net	111,134	1,806
Cash flows from operating activities	841,207	337,669
CASH FLOWS USED FOR INVESTING ACTIVITIES		
Sales, maturities, prepayments and scheduled redemption of:		
Invested assets *(note 27)*	1,749,077	1,766,824
Policy loans	15,619	18,908
Purchase / issue of:		
Invested assets *(note 27)*	(2,526,639)	(2,179,827)
Policy loans	(10,332)	(14,232)
Property and equipment	(26,392)	(29,481)
Subsidiary, net of cash acquired	–	(179,760)
Cash flows used for investing activities	(798,667)	(617,568)
CASH FLOWS FROM (USED FOR) FINANCING ACTIVITIES		
Issue of Second preferred shares, Series 3	96,796	–
Issue of subordinated debt *(note 14)*	–	100,000
Contributed surplus	–	95,000
Dividends paid	(7,148)	(7,620)
Cash flows from (used for) financing activities	89,648	187,380
Increase (decrease) in cash and cash equivalents	132,188	(92,519)
Cash and cash equivalents, beginning of year	88,002	180,521
Cash and cash equivalents, end of year *(note 27)*	$ 220,190	$ 88,002

See accompanying notes to financial statements

Segregated Funds
Consolidated Statements of Changes in Net Assets

as at December 31, 2002 and 2001 (in thousands of Canadian dollars)

	2002	2001
Segregated fund assets, beginning of year	$ 5,787,578	$ 4,664,464
Increase during the year		
Acquisition of funds *(note 3)*	–	1,030,093
Amounts received from policyholders	1,687,055	1,509,419
Amounts transferred to the General Fund	4,280	3,910
Interest income	84,034	92,849
Dividends	46,641	36,357
Net realized loss on sale of investments	(334,667)	(223,999)
Net unrealized decrease in market value of investments	(381,020)	(26,107)
	1,106,323	2,422,522
Decrease during the year		
Amounts withdrawn by policyholders	(1,573,321)	(1,184,153)
Management fees and other operating costs	(119,088)	(98,997)
Distributions paid	(31,421)	(16,258)
	(1,723,830)	(1,299,408)
Segregated fund assets, end of year	$ 5,170,071	$ 5,787,578

See accompanying notes to financial statements

Segregated Funds
Consolidated Statements of Net Assets

as at December 31, 2002 and 2001 (in thousands of Canadian dollars)

	2002	2001
Segregated fund assets consist of:		
Cash and short-term investments	$ 907,449	$ 1,131,974
Bonds	980,631	978,901
Mortgages	430	3,901
Equities	2,413,023	2,636,441
Units of other funds	868,538	1,036,361
	$ 5,170,071	$ 5,787,578

See accompanying notes to financial statements

Notes to Consolidated Financial Statements

Years ended December 31, 2002 and 2001 (in thousands of Canadian dollars)

The Maritime Life Assurance Company (the "Company") is continued under the Insurance Companies Act. *It operates in the Canadian financial services industry and operations cover the development and marketing of individual life insurance and living benefits, investment products, pensions, institutional annuities and group life and health products and services.*

The Company is subject to regulation by the Office of the Superintendent of Financial Institutions Canada ("OSFI"). Under regulations and guidelines prescribed by OSFI, the Company is required to maintain prescribed levels of capital that are dependent on the type and amount of insurance policies in force and the nature of the Company's assets. The Company currently exceeds these minimum capital requirements. OSFI governs the distribution of the Company's earnings through monitoring of adherence to prescribed capital requirements.

1. Significant accounting policies and basis of presentation

The significant accounting policies used in the preparation of these consolidated financial statements, including the accounting requirements of OSFI, are summarized below. These accounting policies conform, in all material respects, to generally accepted accounting principles.

Basis of presentation

These consolidated financial statements have been prepared in accordance with Subsection 331(4) of the *Insurance Companies Act* which states that, except as otherwise specified by OSFI, the financial statements are to be prepared in accordance with generally accepted accounting principles and include the accounts of its wholly owned subsidiary Landex Properties Ltd. The comparative period included the accounts of Royal & Sun Alliance Life Insurance Company of Canada ("RSAF"). RSAF was acquired on October 1, 2001 and accordingly, the results of the operations from that date have been included in these consolidated financial statements *(see note 3)*. RSAF and the Company were amalgamated on January 1, 2003 to carry on operations as The Maritime Life Assurance Company.

Bonds and mortgages

Bonds and mortgages are carried at amortized cost, net of any allowance for losses. The difference between the proceeds on the sale of a security and its amortized cost is considered to be an adjustment of future portfolio yield and is deferred on the balance sheet and amortized to income over the remaining term to maturity.

The Company ceases to accrue interest on loans that are three months or more in arrears and considers these loans to be impaired as well as any loans that are deemed by management to be non-performing. Events and conditions considered in determining the charge to income during the year relating to the allowance for loan impairment include the value of the security underlying the loan, geographic location, industry classification of the borrower, an assessment of the financial stability of the borrower, repayment history and an assessment of the impact of the current economic conditions. Impaired loans are valued at an amount equal to the estimated net cash flows receivable, discounted at the effective interest rate inherent in the loan at the time of impairment. Any write-down is recognized immediately in income as a charge for loan impairment.

Upon restructuring, impaired loans are recorded at an amount equal to the net cash flows receivable under the modified terms, discounted at the effective interest rate inherent in the loan at the time it was initially recognized as being impaired. Any reduction in the recorded investment is recognized in income as a charge for loan impairment. When collection of the scheduled future cash flows is reasonably assured, interest income is recognized, using the above inherent effective interest rate.

Equities

The majority of the Company's equity holdings match equity-related investment options available with certain universal life insurance products. These holdings include groups of common stocks, index futures, index participation units and externally managed equity funds. These equity-related assets are accounted for on a market value basis in order to match the market value of the liability.

The remaining equities are carried at moving average market value whereby the carrying value is adjusted towards market value at 5% per quarter. Net realized gains and losses on the disposal of equities are deferred and amortized to income at 5% per quarter on a declining balance basis. A decline in market value of the portfolio of equities that is considered to be other than temporary is recognized immediately.

Real estate

Real estate held for investment, which includes own-use property, is carried at moving average market value whereby the carrying value is adjusted towards market value at 3% per quarter. Net realized gains and losses are deferred and amortized to income at 3% per quarter on a declining balance basis. Market values on each property are determined annually and an independent appraisal is obtained every three years. The market value established is an estimate of the realizable value of each property and thus recognizes in that determination an element of depreciation. A decline in market value of the portfolio of real estate that is considered to be other than temporary is recognized immediately.

Real estate acquired on foreclosure and held for sale is carried at the lower of the investment in the loan foreclosed and the estimated net proceeds from sale of the property. Real estate acquired on foreclosure and held for income production is initially recorded at the lower of the investment in the loan foreclosed and the fair value of the assets. Subsequently, foreclosures held for income production are accounted for as investments. For both classifications, write-downs are recognized immediately in income as a charge for loan impairment in the year.

Policy loans

Policy loans are carried at unpaid principal balances and are secured by the cash surrender values of the policies against which the respective loans were made.

Goodwill

The excess of cost over the fair value of the net assets of businesses acquired (goodwill) is included in the consolidated balance sheet. Goodwill relating to acquisitions completed before July 1, 2001 was amortized on a systematic basis over a period considered to be its estimated useful life of 20 years. Goodwill acquired after July 1, 2001 is not subject to amortization and amortization has ceased for all

goodwill commencing January 1, 2002. Commencing in 2002, all goodwill is subject to an annual impairment review. Impaired goodwill will be charged to income in the year the impairment is identified.

Derivative financial instruments

The Company uses various derivative instruments to hedge and manage its exposure to changes in interest rate levels, foreign exchange rates, and equity market prices and to manage the duration of assets and liabilities.

In certain cases, the Company uses hedge accounting, in accordance with Section 1650 of the *CICA Handbook*, by designating derivative instruments as a hedge in accordance with its risk management objective and strategy. For derivatives that are designated and qualify as a hedge, changes in its fair value or cash flows are netted against the changes in the fair value or cash flows of the underlying hedged item.

The Company enters into hedges of its foreign currency exposures on foreign currency denominated investments and intercompany debt by entering into currency swaps, currency futures, and forward exchange contracts when it is deemed appropriate.

Foreign exchange translation gains and losses on foreign currency denominated derivative financial instruments used to hedge foreign currency investments or debt are accrued under the respective invested asset or debt category on the balance sheet and recognized currently in net investment income or interest expense on the income statement, offsetting the respective translation gains or losses recognized on the underlying hedged item.

The Company also enters into interest rate swaps in order to reduce the impact of fluctuating interest rates on its floating rate invested assets and policy liabilities. These swap agreements require the periodic exchange of payments without the exchange of the notional principal amount on which the payment is based. The Company designates its interest rate hedge agreements as hedges of the underlying asset or liability. Interest income or expense is adjusted to include the payments made or received under the interest rate swaps.

Hedge effectiveness is assessed quarterly. If a hedge becomes ineffective, the hedge accounting described above ceases and the derivative instrument is recognized on the balance sheet at its fair value. Changes in the fair value of derivatives that are not hedges are included in net realized investment gains (losses) in the income statement.

Other assets

Other assets include furniture, equipment, leasehold improvements, software and limited life intangible assets that are carried at cost less accumulated depreciation. Depreciation is provided on a straight-line basis over periods from three to ten years.

Policy liabilities

Policy liabilities have been calculated using the Canadian Asset Liability Method in accordance with the standards of the Canadian Institute of Actuaries ("CIA"). The process of calculating policy liabilities necessarily involves the use of estimates concerning such factors as mortality and morbidity rates, future investment yields, future investment losses, future expense levels and rates of surrender. Consequently,

policy liabilities include appropriate provisions for adverse deviations from those estimates.

Revenue recognition

Premiums from participating and non-participating individual life insurance and annuity policies are recognized as income when due. Premium and administration fees for Group life and health contracts are recognized over the period services are rendered. Investment management fees are calculated daily for assets under administration based on their closing market values. Administration fees for pension contracts are calculated monthly based on the number of members in the plan. Investment advisory and service fees are recognized as revenue when services are performed. Commissions related to security transactions are recognized as income on the trade date.

Foreign currency translation

The assets and liabilities denominated in foreign currencies are translated into Canadian dollars at rates in effect at the balance sheet date. Revenues and expenses are translated at the average exchange rates prevailing during the year. Translation gains and losses are recognized in the income statement.

Income taxes

Income taxes are accounted for using the liability method of income tax allocation. Under this method, current income taxes are based on taxable income and future income taxes are based on temporary differences between the tax basis and book basis of assets and liabilities. The income tax rates used to measure income tax assets and liabilities are those rates substantively enacted at the balance sheet date.

A valuation allowance is established for future tax assets when it is more likely than not that an amount will not be realized.

Pension expense and obligation

The Company provides certain pension and other future post-employment benefits to eligible participants upon retirement. These benefits are provided on both defined benefit and defined contribution bases and reflect compensation history, length of service and level of contributions. The cost of defined benefits is actuarially determined and accrued using the projected benefit method pro-rated on service. This method involves the use of management's best estimates concerning such factors as expected plan investment performance, future salary increases, retirement ages of plan members and expected health care costs. These costs are recognized in the consolidated statement of income in the period during which the services are rendered. Plan assets are carried at market values. The assets supporting the pension benefits are held in separate trusteed pension funds.

The estimated excess of the market value of plan assets over retirement obligations, including adjustments arising from plan amendments and changes in valuation assumptions, is included in income over the estimated average remaining service lives of participants. The excess of the net actuarial gain (loss) over 5% of the greater of the benefit obligation and the fair value of the plan assets is amortized over the remaining service period of active participants.

The cumulative difference between the pension expense and the funding contributions for the pension benefits is recorded in the consolidated

balance sheet under other assets. The accumulated value of other employee future benefits is recorded in the consolidated balance sheet as other liabilities.

Segregated fund assets

Certain policy contracts allow the policyholder to invest in segregated investment funds of the Company. The assets of these funds are carried at their year-end market values. The income for these funds includes all realized and unrealized gains and losses, net of related expenses and is included in the value of the fund. Substantially all risks and rewards of ownership accrue to these policyholders; consequently, assets held in segregated fund accounts are not consolidated with the assets of the Company. Cash flows associated with premiums and surrenders of segregated fund policies are initially recorded in the general account and then transferred to or from the segregated account on a net basis so that the segregated accounts business is maintained separately from the general account business.

The Company provides certain minimum maturity and death benefit guarantees on individual variable annuity contracts which have invested in segregated investment funds. The liability associated with these guarantees is included with the policy liabilities *(see note 9)*.

2. Changes in Accounting Policies

Business combinations

The Company has adopted Section 1581, "Business Combinations", of the *Canadian Institute of Chartered Accountants* ("CICA") *Handbook* effective July 1, 2001. This standard requires the use of the purchase method of accounting for acquisitions and provides additional guidance in connection with the allocation of the purchase price to net assets including intangibles and goodwill.

Goodwill and other intangible assets

The Company has adopted Section 3062, "Goodwill and Other Intangible Assets", of the *CICA Handbook*, effective July 1, 2001. Under the transitional provisions of this accounting standard, goodwill acquired after the effective date will not be subject to amortization. Commencing in 2002, amortization will also cease for previously acquired goodwill. Also commencing in 2002, all goodwill will be subjected to an annual impairment review. Impaired goodwill will be charged to income in the year the impairment is identified.

Stock-based compensation

The Company has adopted Section 3870, "Stock-Based Compensation and Other Stock-Based Payments", of the *CICA Handbook* effective January 1, 2002. The new standard requires that all compensatory awards, including stock appreciation rights, be measured using the fair value method at the grant date and recognized as compensation expense over the service period. The impact of this change is not material to these consolidated financial statements.

Hedging relationships

In November 2001, the CICA issued Accounting Guideline 13, *Hedging Relationships*, effective for fiscal years beginning on or after July 1, 2003, which requires the identification, documentation, designation and determination of effectiveness of a hedging relationship to apply hedge accounting. The new guideline also outlines conditions whereby hedge accounting for hedging relationships established in prior periods can be continued. The Company does not expect the impact of this Guideline to be material to these consolidated financial statements.

3. Acquisition and Goodwill

On October 1, 2001, the Company acquired 100% of the issued and outstanding shares of RSAF for cash consideration of $237,641, including costs of the transaction of approximately $1,000.

The acquisition was accounted for by the purchase method. Accordingly the purchase price was allocated to the assets and liabilities acquired, based on their estimated fair values at the acquisition date.

The effect of the purchase accounting and the comprehensive revaluation adjustments on the carrying values of the acquired assets and liabilities was as follows:

RSAF Summary Balance Sheet	September 30 2001	Revaluation Adjustments	October 1 2001
Invested assets	$ 961,694	$ 105,428	$ 1,067,122
Premiums receivable and other assets	54,456	(11,124)	43,332
Goodwill	–	105,718	105,718
Total assets	$ 1,016,150	$ 200,022	$ 1,216,172
Policy liabilities	$ 819,218	$ 136,685	$ 955,903
Other liabilities	27,572	(2,024)	25,548
Deferred gains	22,687	(22,687)	–
Participating account	1,170	(4,090)	(2,920)
Shareholders' equity	145,503	92,138	237,641
Total liabilities and shareholders' equity	$ 1,016,150	$ 200,022	$ 1,216,172

As part of the purchase negotiation, the Company agreed to enter into an investment management agreement with a company related to the Vendor. This agreement provides that the investment services will be rendered at a fee based on regular commercial terms subject to a $1,000 minimum fee per year over the next six years. Should this agreement terminate before six years have elapsed, the remaining minimum fees will be payable immediately.

The goodwill was allocated to the non-participating fund, and was not subject to amortization in accordance with the transitional rules of Section 1581 "Business Combination" *(see note 2)*.

In addition, RSAF managed segregated funds that had an aggregate fair market value at October 1, 2001 of $1,030,093.

RSAF and the Company amalgamated on January 1, 2002 to carry on business as The Maritime Life Assurance Company.

Goodwill

The continuity of goodwill during the year was as follows:

2002	Retail Protection	Asset Gathering	Group Life & Health	Total
Balance, beginning of year	$ 114,565	$ 49,177	$ 70,300	$ 234,042
Acquired during the year	–	–	–	–
Amortization during the year	–	–	–	–
Balance, end of year	$ 114,565	$ 49,177	$ 70,300	$ 234,042

2001	Retail Protection	Asset Gathering	Group Life & Health	Total
Balance, beginning of year	$ 52,445	$ 9,406	$ 75,008	$ 136,859
Acquired during the year	65,357	40,361	–	105,718
Amortization during the year	(3,237)	(590)	(4,708)	(8,535)
Balance, end of year	$ 114,565	$ 49,177	$ 70,300	$ 234,042

4. Invested assets and fair values

Fair value amounts represent estimates of the consideration that would currently be agreed upon between knowledgeable, willing parties under no compulsion to act. Although quoted market values are a good source of fair value, not all financial instruments have an available trading market. In addition, fair value refers to value at a point in time and is not indicative of future value.

The Company's business involves the exchange of financial instruments. A financial instrument is defined as any contract that gives rise to both a financial asset of one party and a financial liability or equity instrument of another party. A basic function of the business is to match assets with liabilities to be able to meet the long-term obligations to policyholders.

The fair values of the policy liabilities cannot practicably be determined. To the extent that invested assets are accurately matched to policy liabilities, changes in the fair values of the assets due to interest rate changes will have a similar effect on the policy liabilities and will not affect future corporate earnings. The assets supporting the policy liabilities have a fair value of $7,695,553 (2001 - $6,871,155). In addition, deferred net gains of $40,058 (2001 - $29,361) have been taken into account in the determination of policy liabilities. Details of significant terms and conditions, exposures to interest rate and credit risks on policy liabilities are discussed in note 9.

The following indicates the fair value and the carrying value of the Company's invested assets at December 31. Although real estate is not a financial instrument, it has been included in the table for completeness. For derivatives, see note 7. The fair values shown are not indicative of the overall fair value of the Company.

Asset valuation

The fair values of short-term investments are estimated to be carrying value due to the nature of these assets. Fair values of bonds and equities are derived from available quoted sources where a ready market exists.

The fair values of mortgages and private placement bonds and equities are calculated by discounting

scheduled cash flows through the estimated maturity, using market discount rates. Fair values for real estate are based on the most recent independent appraisal available *(see note 1)*.

		2002 Fair Value	2002 Carrying Value	2001 Fair Value	2001 Carrying Value
ASSETS					
Bonds	– government	$ 1,938,533	$ 1,734,134	$ 1,904,853	$ 1,839,559
	– public	2,005,873	1,925,796	1,595,641	1,558,714
	– private placements	1,259,277	1,129,035	1,031,881	932,373
Mortgages	– government insured	1,179,377	1,142,511	1,051,491	1,027,880
	– commercial	1,017,916	986,098	920,188	900,150
	– multi-residential	232,389	225,125	191,334	187,414
Equities	– preferred	313,430	314,770	334,962	334,470
	– common	109,402	107,364	95,398	92,380
	– private placements	46,638	42,396	49,152	45,687
	– other	454,379	455,329	462,664	462,664
Real estate	– foreclosed	306	306	1,145	845
	- investment	151,066	140,689	140,304	126,227
Short-term investments		304,890	304,890	120,097	120,097

Short-term investments

These investments have an aggregate amount of $304,890 (2001 - $120,097) with effective interest rates of 1.27% to 3.31% (2001 - 1.61% to 5.63%). Interest is calculated daily and receivable at maturity or on disposition.

Bonds

Interest is calculated daily and paid semi-annually on government and public bonds. Private placement bonds have interest calculated and paid according to specific contracts. Exposure to credit risk is managed primarily through compliance with quality rating, maximum single issuer guidelines and industry exposure guidelines.

	2002 Effective Rates	2002 Carrying Value	2001 Effective Rates	2001 Carrying Value
Government	5.60%	$ 1,734,134	5.90%	$ 1,839,559
Corporate	5.60%	3,054,831	5.79%	2,491,087

The term to maturity for bond investments, which generally match estimated liability maturities, are as follows:

Term to maturity	2002 Fair value	2002 Carrying Value	2001 Fair Value	2001 Carrying Value
Current	$ 287,184	$ 277,592	$ 199,816	$ 185,173
1-5 years	1,074,425	1,040,378	909,825	884,541
6-10 years	780,586	742,131	679,279	669,388
Over 10 years	3,061,488	2,728,864	2,743,455	2,591,544
	$ 4,203,683	$ 4,788,965	$ 4,532,375	$ 4,330,646

Mortgages

Interest is generally calculated monthly. Credit risk is managed through a program of diversification of type and location of properties, maximum single borrower guidelines and regular borrower and appraisal reviews.

			2002			2001
	Carrying Amount	Effective Interest Rates	Average Maturity (years)	Carrying Amount	Effective Interest Rates	Average Maturity (years)
Government insured	$ 1,142,511	6.57%	7.92	$ 1,027,880	6.92%	6.75
Commercial	986,098	6.92%	7.13	900,150	7.77%	8.52
Multi-residential	225,125	7.48%	5.77	187,414	7.22%	4.95
	$ 2,353,734			$ 2,115,444		

Mortgages are secured primarily by first recourse to the underlying property and virtually all are fixed term in duration.

5. Impaired investments

Investments classified as non-performing are as follows:

			2002			2001
	Book Value	Allowance for Loan Impairment	Carrying Value	Book Value	Allowance for Loan Impairment	Carrying Value
Commercial mortgages	$ 5,936	$ (578)	$ 5,358	$ 19,965	$ (1,450)	$ 18,515
Bonds	21,796	(7,789)	14,007	6,291	(3,777)	2,514
	$ 27,732	$ (8,367)	$ 19,365	$ 26,256	$ (5,227)	$ 21,029

In addition, the policy liabilities include provisions for potential future asset default losses *(see note 9)*.

The continuity of the allowance for loan impairment during the year was as follows:

	2002	2001
Balance, beginning of year	$ 5,227	$ 10,960
Provision for loan impairment	4,352	31
Reduction due to dispositions	(1,429)	(4,868)
Net write-offs (recoveries) of loans	217	(896)
Balance, end of year	$ 8,367	$ 5,227

6. Other assets

At December 31, other assets consist of:

	2002	2001
Furniture and equipment	$ 123,916	$ 116,645
Leasehold improvements	3,603	2,654
Internal use software development	41,810	24,383
Intangible assets	4,750	6,000
Less: accumulated depreciation and amortization	(107,439)	(92,075)
	66,640	57,607
Advances to segregated funds	17,795	10,755
Deferred pension costs *(note 23)*	20,496	25,007
Income taxes receivable	–	4,605
Administration services receivable	11,343	17,879
Recoverable deficits	14,140	46,962
Miscellaneous receivables	84,517	63,295
	$ 214,931	$ 226,110

7. Derivative financial instruments

The Company uses derivative financial instruments where appropriate in the administration of its asset/liability management strategies and to assist in the management of financial risks, including interest rate and foreign exchange risks. All of the Company's derivative financial instruments are held for hedging purposes, not for speculation.

The notional principal amount of derivative instruments represents an amount to which a rate or price is applied in order to calculate the exchange of cash flows. Notional principal amounts are frequently used as an indicator of business activity, however, they are not indicative of credit or market risk exposure and are not recognized in the financial statements. The following table classifies, by type, the notional principal amounts held at year end:

	2002		2001	
	OTC*	Exchange	OTC*	Exchange
Interest rate contracts				
Swaps	$ 760,583	$ –	$ 119,992	$ –
Foreign exchange contracts				
Swaps	440,383	–	73,303	–
Forward rate agreements	104,333	–	117,539	–
Equity contracts	8,000	21,470	8,800	19,187
	$ 1,313,299	$ 21,470	$ 319,634	$ 19,187

"Over-the-counter"

The notional principal amounts by remaining term to maturity are:

	Remaining term to maturity at December 31, 2002				2002 Total Notional Amount	2001 Total Notional Amount
	Within 1 year	1 to 5 years	5 to 10 years	Over 10 years		
Interest rate contracts	$ 83,000	$ 351,877	$ 167,649	$ 158,057	$ 760,583	$ 119,992
Foreign exchange contracts	114,171	394,230	21,293	15,022	544,716	190,842
Equity contracts	24,470	5,000	–	–	29,470	27,987
	$ 221,641	$ 751,107	$ 188,942	$ 173,079	$1,334,769	$ 338,821

Credit exposure

Credit risk is the exposure to loss in the event of non-performance by the counterparty to the transaction. The Company evaluates and monitors the credit risk of its derivative financial instruments, in much the same way as the credit risks associated with its other financial instruments. All of the counterparties for the Company's OTC derivative activities are financial institutions rated AA(L) or above by independent rating agencies.

The following tables provide a summary of the Company's derivative portfolio and related credit risk exposure. "Current credit risk" represents the amount of loss that the Company would suffer if every counterparty to which the Company is exposed defaulted immediately (i.e. the current replacement cost of all outstanding derivative contracts with a gain or positive value). These amounts do not take into consideration legal contracts that permit offsetting of positions or the value of any collateral. "Credit equivalent" amount represents the current credit risk exposure plus an estimate of the impact that future changes in interest and foreign currency rates and other indices would have, based upon a formula prescribed by OSFI. "Risk-weighted equivalent" represents the credit risk equivalent weighted according to the creditworthiness of the counterparty, also as prescribed by OSFI.

2002	Notional Amounts	Current Credit Risk	Credit Equivalent Amount	Risk Weighted Equivalent
Interest rate contracts	$ 760,583	$ 12,473	$ 3,426	$ 79
Foreign exchange contracts	544,716	4,740	8,663	200
Equity contracts	29,470	924	1,504	24
	$1,334,769	$ 18,137	$ 13,593	$ 303

2001	Notional Amounts	Current Credit Risk	Credit Equivalent Amount	Risk Weighted Equivalent
Interest rate contracts	$ 119,992	$ 3,910	$ 1,768	$ 28
Foreign exchange contracts	190,842	133	1,967	31
Equity contracts	27,987	1,934	2,249	36
	$ 338,821	$ 5,977	$ 5,984	$ 95

The next table summarizes the fair value, as represented by the sum of the net unrealized gains and losses, accrued interest receivable and payable and premiums paid or received, of the Company's derivative portfolio at each year end. It segregates derivative instruments between those that are in a favourable or receivable position from those in an unfavourable or payable position. Fair value is verified to external sources and is defined as the net present value of expected future cash flows of all contracts discounted at a market rate commensurate with the risks involved.

			2002			2001
	Favourable	(Unfavourable)	Net Fair Value	Favourable	(Unfavourable)	Net Fair Value
Interest rates contracts	$ 12,473	$ (36,085)	$ (23,612)	$ 3,910	$ (513)	$ 3,397
Foreign exchange contracts	4,740	(14,975)	(10,235)	133	(10,772)	(10,639)
Equity contracts	924	(610)	314	1,934	(111)	1,823
	$ 18,137	$ (51,670)	$ (33,533)	$ 5,977	$ (11,396)	$ (5,419)

8. Mortgage securitization

The Company has sold for cash, without recourse, undivided interests in pools of mortgages insured under the *National Housing Act* by the Government of Canada. Gains or losses on the sale of the mortgages are amortized to income over the life of the underlying mortgage pools and are recognized within net investment income.

The Company retains the servicing right for these pools of mortgages that had outstanding principal balances of $188,447 (2001 - $199,163) at December 31. Servicing fee income, net of expenses, is recognized as earned and recorded within net investment income.

9. Policy liabilities

a) Nature and composition

Policy liabilities represent the amounts that, together with estimated future premiums and investment income, will be sufficient to pay estimated future benefits, policy dividends and expenses on policies in force at the valuation date. Policy liabilities are determined using accepted actuarial practice, according to standards established by the CIA.

The Company's reporting segments are described in note 26. The composition of the policy liabilities, net of reinsurance *(see note 10)* and the assets backing them by segment are as follows:

2002	Retail Protection	Asset Gathering	Group Life & Health	2002 Total
Participating policies	$ 813,101	$ 2,445	$ –	$ 815,546
Non-participating policies	2,863,975	2,151,436	1,405,122	6,420,533
Total policy liabilities	$3,677,076	$2,153,881	$1,405,122	$7,236,079
Assets backing liabilities:				
Bonds	$2,309,928	$1,325,484	$ 625,658	$4,261,070
Mortgages	700,934	826,046	734,431	2,261,411
Equities	503,185	7,334	–	510,519
Other	163,029	(4,983)	45,033	203,079
	$3,677,076	$2,153,881	$1,405,122	$7,236,079

2001	Retail Protection	Asset Gathering	Group Life & Health	2001 Total
Participating policies	$ 790,289	$ 2,580	$ –	$ 792,869
Non-participating policies	2,638,619	1,775,124	1,423,303	5,837,046
Total policy liabilities	$3,428,908	$1,777,704	$1,423,303	$6,629,915
Assets backing liabilities:				
Bonds	$2,183,456	$1,024,200	$ 657,603	$3,865,259
Mortgages	681,965	702,520	696,451	2,080,936
Equities	519,369	–	–	519,369
Other	44,118	50,984	69,249	164,351
	$3,428,908	$1,777,704	$1,423,303	$6,629,915

b) Assumptions

The Company provides financial security products and must measure and manage risk. This is reflected in the valuation of policy liabilities. In light of the long-term risks and measurement uncertainties inherent in the life insurance business, policy liabilities are established using "best estimate" assumptions plus a margin for adverse deviation, separately for each variable. If emerging experience is less favourable than assumed in the valuation, profits would diminish and losses could result.

"Best estimate" assumptions cover mortality, morbidity, investment returns, rates of policy terminations (lapses), levels of operating expenses, and policyholder dividends. The methods for arriving at the most important of these assumptions are outlined below.

Mortality

For individual life insurance, the Company monitors its mortality on a regular basis and compares the results to the Canadian industry study conducted annually by the CIA. The valuation mortality assumption has been derived from a combination of the Company's experience and industry experience. Although mortality improvements have been observed for many years, no future improvements have been assumed for life insurance valuation.

For annuities, the mortality rates in the industry tables are projected forward to the year of each future annuity payment to allow for continuing mortality improvement. This is an appropriately conservative adjustment to make in valuing annuities — it extends the assumed payment period which produces a larger policy liability.

Morbidity

The Company underwrites disability income, disability waiver of premium and other living benefits. The Company's exposures to morbidity risk arise from the possibilities that the incidence of claims is greater or earlier than expected and, where relevant, claim terminations from death or recovery occur less frequently than expected.

The Company uses a combination of industry tables and its own recent experience in setting its best estimate claims incidence and termination.

Investment returns

The Company maintains notional asset portfolios matching specific segments of policy liabilities. This allows management to monitor and assess the success of the various investment strategies being employed. All assets in the Company's general fund are available to pay all liabilities of the general fund, with first preference to policy liabilities.

The Company has an Investment Policy Statement ("IPS") which, coupled with the Investment Operating Guidelines ("IOG"), articulate prudent person practices for its lending and portfolio management — practices a prudent person would apply to avoid undue risk of loss and to obtain a reasonable rate of return. The IPS is approved by the Board of Directors and is subject to annual review. The IOG are approved by the Investment Committee of the Board. These documents outline governance with respect to exposure limits, credit quality, interest rate risk and liquidity. The valuation of policy liabilities makes explicit provision for credit risk and interest rate risk.

i) Credit risk

The Company has made provision in its financial statements for credit losses expected for assets it currently holds. Provisions have been made partly through reduction in the value of specific assets judged to be impaired and partly through a provision in the policy liabilities. The best estimate assumptions take into account current quality ratings for all investments, credit analysis, quality deterioration (ratings drift) and economic indicators that are considered linked to credit risk that may be cyclical.

The Company reviews its own experience and published credit loss studies to develop and maintain best estimate long term credit loss allowances for each distinct asset credit class. The policy liabilities produced using these allowances may be supplemented if credit analysis, economic trends or business plan forecasts indicate that credit losses are likely to be higher, in the near term, than the average of the long term allowances.

Actual credit losses were lower than best estimate losses assumed in the valuation of policy liabilities in each of the last four years.

The policy liabilities would increase by 1.10% (2001 - 1.02%) if the long-term credit loss assumption was increased to 150% of the assumption used.

ii) Interest rate risk

The Company's financial position may be affected by its exposure to interest rate risk. Interest rate risk is the risk of economic losses or gains arising from the reinvestment or disinvestment of cash flows. If the assets supporting the policy liabilities do not match the timing and amount of the policy obligations, interest rate losses or gains may occur due to changing interest rates in the future. The Company has an asset/liability management program that achieves an effective match.

Under the Canadian Asset Liability Method ("CALM") of the CIA, interest rate risk for each broad product class is assessed under an appropriately chosen variety of future economic scenarios. The selection of the scenarios tested is guided by standards, portfolio-specific attributes and judgment. In selecting the scenarios, the objective is to determine a provision for interest rate risk that is sufficient without being excessive. For each scenario and class, the analysis determines the pool of existing assets which, when combined with assumed future reinvestments or disinvestments of projected net cash flows at rates defined by the scenario, is sufficient to discharge the liability cash flows. The provision for interest rate risk is then determined based on the retained scenario, which requires the largest pool of existing assets i.e. the worst case scenario.

The asset gathering segment is most sensitive to immediate changes in interest rates. For this segment, asset and liability cash flows are closely matched by term and duration so the reinvestment assumption is relatively unimportant. The objective is to maintain asset durations within 10% of liability durations for this segment. At December 31, 2002, these segments are adversely exposed to increases in interest rates because the assets are slightly longer than the liabilities. For these policy liabilities, the difference between the scenario assuming a 1% increase in interest rates at all points along the yield curve and the scenario assuming the current yield curve forever is $800 (2001 - $1,600) or 0.03% (2001 – 0.09%) of the policy liabilities reported.

For guaranteed non-participating insurance, benefit payments are typically later than asset cash flows which means that reinvestment assumptions are important to the valuation of this class of business. This exposure is reflected in the valuation of the policy liabilities by assuming declining long term interest rates. Projected policy cash flows and invested assets' cash flows are combined with the future assumed reinvestment rates and the Company's investment policy to determine the policy liability.

For adjustable product types, including deferred annuities, certain forms of universal life, participating policies and some group contracts, the effect of changes in interest rates will be passed through to policyholders in the form of changes in dividend scales or premium adjustments or credited rates in accordance with the policy terms. These pass-through features significantly reduce the Company's exposure to interest rate risk.

The Company offers some universal life policyholders the opportunity to invest in equity-related investment options. These investment accounts are closely matched using various equity instruments — actual common stocks, equity futures or exchange-traded unit trusts.

iii) Product performance guarantees

The Company guarantees minimum rates of return with respect to the savings elements of adjustable and universal life insurance policies. These guarantees create a cost to the Company (are "in the money") whenever its investment strategy produces a return which is less than the sum of the guaranteed minimum returns payable to customers and its investment spread related costs. Some of the Company's outstanding guarantees were "in the money" at December 31, 2002. Guarantees for recent and future new issues have been revised so that the Company's future exposure will largely be limited to an existing closed block of inforce policies. The valuation of policy liabilities assumes "in the money" situations persist and incorporates a margin for future deterioration.

For segregated funds, the Company guarantees minimum proceeds on the maturity date of the policy or on the earlier death of the annuitant. These guarantees exceed those that the Company must provide as defined by regulations. The Company regularly monitors its exposure to these guarantees and measures their costs under a wide range of future fund performance scenarios (both randomly generated and predefined). The key risk to which the Company is exposed is very poor fund(s) performance combined with uncharacteristically good persistency. The product design and marketing focus have produced a widely dispersed maturity date profile for the inforce business that provides important diversification and risk mitigation. The policy liabilities include an amount for these guarantees. The method of determining this amount conforms with the approach described in guidance material published by the CIA.

Lapses

Lapse and surrender assumptions are important in valuing individual life insurance because the surrender value of a policy (Cash Surrender Value) can often be quite different than the value of future benefits to be derived by continuing the policy in force. This is most evident with a pure "Term to 100" policy which has no cash surrender value but has inherent increasing value as the policy ages because the premium is fixed based on the issue age. Such a policy is often referred to as lapse-supported.

The Company derives lapse and surrender assumptions mainly from internal studies, in combination with meaningful inter-company studies where available, adjusted for consistency with the future expected economic and mortality environment described above. Separate lapse assumptions are used for permanent cash value business, for renewable term insurance and for lapse-supported business.

The Company has a portfolio of lapse-supported life policies which account for \$2,409,000 (2001 - \$2,179,000) of policy liabilities. As an indication of the sensitivity of these policy liabilities to the future assumed lapse rates, the lapse component of the Minimum Continuing Capital and Surplus Requirement regulatory capital calculation attributable to these policies is \$48,000 (2001 - \$44,000). This component is determined by recalculating the policy liabilities using more conservative lapse rates, with the change in lapse rates being twice as great for fully guaranteed policies than for adjustable ones.

Policy expenses

The policy liabilities provide for future maintenance expenses, claims adjudication expenses, premium tax, investment income tax, other taxes not integrated with income taxes, reinsurance costs, and renewal commissions to agents.

Policy maintenance expenses are derived from the Company's internal cost allocation studies with no material allowance for anticipated future productivity gains. Expense savings are only recognized after they are realized and demonstrated to be of a permanent nature. Future unit cost rates are assumed to increase with inflation in determining the policy liabilities.

Future income taxes

The Company is required to comply with the standards of both the CIA and the CICA in determining the impact of income taxes. Actuarial standards require that the projected timing of all cash flows associated with the policy liabilities, including income taxes, be included in the determination of the policy liabilities under the Canadian Asset Liability Method.

The policy liabilities are first determined recognizing all related tax effects on a discounted basis, including temporary differences that have already occurred and will reverse in the future and future differences that are projected to occur, both temporary and permanent. Future income tax assets and/or liabilities arising from temporary differences that have already occurred are then computed without discounting. This undiscounted amount is then reclassified from the actuarial liabilities to future income taxes on the balance sheet.

Policyholder dividends

Policy liabilities for participating insurance include the present value of future policyholder dividends. Dividend scales are consistent with the Company's dividend policy, and are assumed to adjust in a manner consistent with future experience assumed.

Margins for adverse deviations

The basic assumptions made in establishing policy liabilities are best estimates for a range of possible outcomes. Companies are required to include a margin in each assumption which increases the policy liability otherwise produced to recognize the uncertainty in establishing these best estimates and to allow for the possible deterioration in experience. A range of allowable margins is prescribed by the CIA. The choice of the margin from this range, characterized as low to high margins, is based on consideration of a number of factors specific to the assumption including: credibility of experience studies, sophistication of the Company's measurement and reaction processes, degree of risk-sharing with the policyholder (i.e. adjustment provisions) and the term of the contract, to name a few. The Company generally maintains margins near the middle of the allowable ranges except where the risk is significantly shared with the policyholder, in which case a lower margin is used.

c) Changes in provision for future policy benefits

Changes in the provision for future policy benefits during the year were caused by the following business activities and changes in actuarial assumptions:

	2002	2001
Balance, beginning of year	$ 6,009,214	$ 4,910,645
Normal changes due to:		
– new policies	505,968	57,934
– inforce policies	222,938	185,439
Acquisition of RSAF *(note 3)*	–	936,324
Group business assumed	–	14,528
Reclassifications among policy liability categories	8,043	(3,626)
Changes in actuarial assumptions and refinements of estimates:		
– non-participating	(63,250)	(77,160)
– participating	(2,120)	(14,870)
Balance, end of year	$ 6,680,793	$ 6,009,214

Valuation assumptions are reviewed and updated annually based on emerging experience. For participating insurance, the changes in assumed future experience affect estimated future dividend amounts. This flow through feature of participating insurance significantly reduces the impact of assumption changes on the policy liabilities.

For non-participating business, the impact of the major assumption changes and refinement of estimates is as follows:

	2002	2001
Assumed future interest rates	$ (9,210)	$ (27,600)
Morbidity	(16,360)	(16,150)
Mortality	13,000	(24,150)
Lapse	29,420	50,840
Maintenance expenses	(3,450)	10,520
Modeling/data corrections	(12,980)	(52,000)
All other	(63,670)	(18,620)
	$ (63,250)	$ (77,160)

10. Reinsurance

The Company reinsures excess mortality, morbidity and lapse exposures on a life insured to limit its loss. It also has catastrophe reinsurance in place to limit the loss it incurs from multiple claims resulting from the same event. The Company's maximum retentions, established separately for individual life, living benefits, group life and group health, are subject to Board approval. Materially all of the reinsurance is ceded to federally registered reinsurance companies operating in Canada.

Reinsurance ceded does not discharge the Company's liability as the primary insurer. Failure of reinsurers to honour their obligations could result in losses to the Company. A contingent liability exists should an assuming company be unable to meet its obligations. The Company evaluates the financial condition of its reinsurers and monitors concentrations of credit risk with its reinsurers to minimize its exposure to losses from reinsurer insolvency.

The amounts shown in the financial statements are net of the following amounts relating to reinsurance ceded:

	2002	2001
Provision for future policy benefits	$ 1,684,663	$ 1,579,305
Premiums	459,267	390,400
Policy benefits	266,644	225,001
Commissions and operating expenses	66,101	63,992

11. Notes payable to reinsurers

The Company has issued notes payable to reinsurers that bear interest at a rate equal to the rate of return on a specified portfolio of assets. At December 31, 2002, the outstanding balance owing under these notes was $94,112 (2001 - $91,935).

12. Deferred net gains

Deferred net gains (losses) on disposal of invested assets is comprised of the following:

	2002	2001
Bonds	$ 40,742	$ 23,607
Mortgages	2,037	2,071
Equities	7,896	11,723
Real estate	(1,493)	(1,684)
	$ 49,182	$ 35,717

13. Other liabilities

At December 31, other liabilities consist of:

	2002	2001
Accounts payable and accrued liabilities	$ 191,734	$ 135,783
Outstanding cheques	21,887	14,770
Administration services payables	39,198	48,163
Post-retirement benefits *(note 23)*	11,013	11,074
Due to reinsurers	–	6,155
Mortgages payable	7,390	8,690
Taxes, licenses, fees payable	33,837	10,050
Accrued interest on subordinated debt	4,851	4,798
Miscellaneous	24,433	13,183
	$ 334,343	$ 252,666

The amounts included in mortgages payable represent charges on real estate that are repayable in varying terms to the year 2003 and bear interest at rates ranging from 6.50% to 6.65% per annum. The payments required to meet mortgage obligations are as follows: 2003 - $1,483; 2004 - $1,148. Interest expense for the year ended December 31, 2002 was $514 (2001 - $678). The fair value of the mortgages payable was calculated by discounting scheduled repayments at current market rates and was estimated to be $7,495 (2001 - $8,619).

14. Subordinated debt

The Company has financed some of its operations through the issue of subordinated debt to its parent, John Hancock Canadian Holdings Limited. The debt is subordinated in right of payment to all policy liabilities of the Company and all other liabilities except those that, by their terms, rank equally with or subordinate to this debt and cannot be repaid without OSFI approval. The debt consists of the following:

Maturity	Interest Rate	2002	2001
October 15, 2007	7.50%	$ 70,000	$ 70,000
July 30, 2014	6.81%	20,000	20,000
October 1, 2014	7.19%	86,000	86,000
April 30, 2016	7.14%	20,000	20,000
September 27, 2016	6.88%	55,000	55,000
October 2, 2016	6.88%	25,000	25,000
		$ 276,000	$ 276,000

The interest is payable semi-annually and total interest expense of $19,874 (2001 - $15,027) related to this debt is included in the statements of income. The fair value of the subordinated debt was calculated by discounting scheduled repayments at current market rates and was estimated to be $291,743 (2001 - $279,244).

15. Distribution of income

Distributions of income to shareholders and to participating policyholders are established by resolutions of the Board of Directors. From time to time, the Board of Directors sets apart a portion of the income of the participating account as safe and proper for distribution as dividends or bonuses. Of the amount set apart, the shareholders are entitled to a portion as specified in the governing statute. The amount eligible for future transfer to shareholders can be transferred only when further dividends are paid to participating policyholders. The cumulative amount eligible for future transfer of $5,433 at December 31, 2002 (2001 - $5,285) is included in the participating account.

The Company has made a commitment to declare dividends in respect of the former Maritime Life and former Aetna Canada participating policies for a five year period at a scale not less than the scale in effect in respect of those policies' anniversaries in 1999, provided that the relevant demographic and economic conditions remain the same as in 1999. Commitments made in respect of dividends for a previously acquired block of participating policies will be honoured by the Company.

Upon amalgamation of the Company and RSAF, the Company further committed to respect pre-existing commitments of dividend scales, including those pertaining to a block of policies acquired by RSAF in 1997. Prior to amalgamation, RSAF reduced the dividend scales of its participating policies to ensure that the RSAF participating fund was self-sustaining. If post-amalgamation experience indicates that further dividend scale reductions are required, the Company has committed to maintain current dividend scales at no less than 80% in aggregate during the five years following amalgamation, except to reflect deterioration in future realized experience, and no reduction will occur while any prior dividend commitment is in effect.

As at December 31, the cumulative amount of $69,837 (2001 - $63,202) of the participating account has been allocated to participating policyholders but has not yet been distributed by way of declared dividends.

16. Share capital

		2002	2001
Authorized			
3,960,000	first preferred shares issuable in series		
4,000,000	second preferred shares, Series 1		
4,000,000	second preferred shares, Series 2		
4,000,000	second preferred shares, Series 3		
5,000,000	common shares		
Issued			
1,400,000	first preferred shares, series A non-voting, cumulative, and redeemable at the Company's option at their par value of $25.00	$ 35,000	$ 35,000
4,000,000	second preferred shares, Series 1	97,106	97,106
4,000,000	second preferred shares, Series 3	96,796	–
350,175	common shares	53,745	53,745
		$ 282,647	$ 185,851

The Second Preferred Shares are non-voting and ranking on a parity with the First Preferred Shares and in preference to the common shares.

The Series 1 Second Preferred Shares bear non-cumulative dividends at a fixed rate of 6.1%, payable quarterly until December 31, 2004 whereupon the dividend rate will be the greater of: (i) one-quarter of 90% of the average daily prime rate charged by two Schedule 1 Canadian chartered banks for that quarter, and (ii) 5.85% per annum, prorated for the quarter. The Series 1 Second Preferred Shares are redeemable at the Company's option on December 31, 2004 and every five years plus one day thereafter at a price of $25.00 per share or at any other time after December 31, 2004 at $25.50 per share. Also on December 31, 2004 and every five years plus one day thereafter the Series 1 Second Preferred Shares are convertible at the holder's option into an equal number of Series 2 Second Preferred Shares, subject to a minimum number of shares remaining in the series.

The Series 2 Second Preferred Shares generally have the same provisions as the Series 1 Second Preferred Shares with the following exceptions. They bear fixed non-cumulative dividends at a rate equal to a selected percentage of the Government of Canada 5 year bond yield, as determined by the Board of Directors, payable quarterly. They are redeemable at the Company's option on January 1, 2010 and on each successive five years plus one day anniversary thereafter. They are convertible by the holder on January 1, 2010 and on each five years plus one day thereafter into an equal number of Series 1 Second Preferred Shares, subject to a minimum number of shares remaining in the series.

The Series 3 Second Preferred Shares, issued on December 13, 2002, bear non-cumulative dividends at a fixed rate of 6.1%, payable quarterly. The Series 3 Second Preferred Shares are redeemable at the Company's option on or after December 31, 2007 at $26.00 per share, on or after December 31, 2008 at $25.75 per share, on or after December 31, 2009 at $25.50 per share, on or after December 31, 2010 at $25.25 per share and on or after December 31, 2011 at $25.00 per share.

17. Institutional annuities business

The Company has entered into agreements whereby the Company may issue annuity contracts to certain investment dealers. The annuity contracts are transferable such that the investment dealers must transfer the purchased annuities to a trust.

The trust, Maritime Life Canadian Funding, expects to issue medium-term notes, and is authorized to issue $1,500,000 of such notes pursuant to a prospectus, to fund the acquisition of the annuities. The trust is a third party qualifying special purpose vehicle whose sole purpose is limited to these activities and accordingly is not subject to consolidation by the Company. Non-consolidation does not remove any liabilities from the Company's balance sheet. The trust has completed two note issues during 2002, resulting in aggregate sales of $350,000 of annuities by the Company.

The annuities are unsecured policy obligations of the Company. Under an elective early final payment option, the policyholder may designate an early final payment date should the Company fail to make any payment when due. In addition, the Company may elect an early final payment date should any change in tax law, regulation, rule or assessment practice occur. If an early termination of the annuity occurs, a final payment amount will be made to settle the annuity in full.

The Company is accounting for these annuities consistent with its existing annuity business in that premiums will be recorded as revenue when received. The annuities will form part of the policy liabilities for the Company and will be subjected to actuarial valuation consistent with the Canadian Asset Liability Method in accordance with the standards of the Canadian Institute of Actuaries. The premiums received will be invested in US and foreign bonds under an investment management agreement with an affiliated company, John Hancock Life Insurance Company.

In addition, the Company has agreed to provide a non-interest-bearing, unsecured, subordinated, limited recourse loan to enable the trust to pay certain of its costs associated with each issue of notes. Accordingly, two loans have been advanced, as follows:

Receivable from:	Maturity	2002
Maritime Life Canadian Funding	January 9, 2004	$ 1,825
Maritime Life Canadian Funding	September 12, 2006	1,173
		$ 2,998

The Company has also provided an indemnity to cover certain unexpected costs and tax liabilities potentially incurred by the trust, the Issuer Trustee and the Indenture Trustee in the future.

18. Investment income

Investment income was derived from the following sources:

	2002	2001
Bonds and debentures	$ 293,285	$ 238,570
Mortgages	156,397	145,688
Equities	(58,627)	(21,058)
Real estate	31,638	29,333
Policy loans	6,830	7,240
Short-term investments	7,755	6,334
Other investment income	(4,792)	(4,039)
Amortization of deferred gains and losses		
Bonds	7,083	4,143
Mortgages	1,107	943
Equities	2,144	2,458
Real estate	1,656	1,577
Investment expenses, including net credit provisions, write-offs and recoveries	(45,563)	(19,633)
	$ 398,913	$ 391,556

19. Unusual items

Unusual items included in the income statement consist of:

	2002	2001
Transition costs associated with RSAF acquisition	$ 9,379	$ 1,109
Integration costs associated with Aetna Canada acquisition	–	16,226
Abandoned office space	–	1,668
	$ 9,379	$ 19,003

20. Income taxes

The income tax expense for the year consists of:

	2002	2001
Current	$ 55,758	$ 10,836
Future	1,130	47,287
	$ 56,888	$ 58,123

The major components of the income tax expense include:

	2002	2001
Current:		
Federal income taxes	$ 45,167	$ 2,791
Federal capital taxes	4,390	4,334
Provincial income taxes	6,201	3,711
	55,758	10,836
Future:		
Federal income taxes	(6,942)	47,763
Provincial income taxes	8,072	(476)
	1,130	47,287
Total income tax expense	$ 56,888	$ 58,123

The provision for income taxes varies from the expected provision at statutory rates for the following reasons:

	2002	2001
Provision for income taxes at statutory rate	38.5%	41.2%
Increase (decrease) from statutory rate:		
Tax exempt investment loss (income)	2.6%	(5.5)%
Capital taxes	3.5%	1.8%
Effect of change in future statutory rates	(0.4)%	(10.3)%
Investment income tax	–	0.2%
Prior years reassessments and adjustments	0.4%	1.6%
Other	1.4%	1.4%
Effective tax rate	46.0%	30.4%

The significant components of the Company's future tax assets and liabilities were as follows:

	2002	2001
Future tax assets:		
Policy liabilities	$ 22,292	$ 32,534
Other assets	(793)	741
Net future tax assets	21,499	33,275
Future tax liabilities:		
Invested assets	$ (148,159)	$ (160,629)
Pension plan	(3,231)	(3,891)
Other	(2,215)	(315)
Net future tax liabilities	(153,605)	(164,835)
	$ (132,106)	$ (131,560)

21. Net income to shareholders

Net income to shareholders has been derived from the following sources:

	2002	2001
Participating business	$ 2,063	$ 1,833
Non-participating business	59,775	108,669
	$ 61,838	$ 110,502

22. Earnings per common share

Earnings per common share ("EPS") is calculated after adjusting net income for the amount of income attributable to preferred shareholders as follows:

	2002	2001
Net income to shareholders	$ 61,838	$ 110,502
Deduct:		
Preferred shareholder dividends	(7,148)	(7,620)
Net income attributable to common shareholders	$ 54,690	$ 102,882
EPS attributable to common shareholders *(in dollars)*	$ 156.18	$ 293.80

23. Future employee benefits

The Company provides pension benefits to substantially all employees. These benefits are provided through three defined benefit pension plans and two defined contribution pension plans. Pension benefits provided under the defined benefit pension plans are based on years of service and average compensation generally during the five years prior to retirement.

The Company also provides medical, dental and life insurance benefits under two closed post-retirement benefit plans.

The total expense for the Company's defined contribution plans is $4,666 (2001 - $4,005).

The changes in benefit obligation and plan assets related to the Company's three defined benefit plans and its two closed other post-retirement benefit plans are summarized as follows:

	Pension Benefits		Other Benefits	
	2002	2001	2002	2001
Change in benefit obligation				
Balance, beginning of year	$ 121,810	$ 109,027	$ 11,074	$ 9,228
Current service cost	3,920	3,067	–	–
Interest cost	7,459	7,744	271	687
Benefits paid	(5,263)	(4,272)	(332)	(361)
Actuarial gains	5,429	–	–	–
Settlement	(26,015)	–	–	–
Acquisition *(note 3)*	–	6,244	–	1,520
Balance, end of year	$ 107,340	$ 121,810	$ 11,013	$ 11,074

	Pension Benefits		Other Benefits	
	2002	2001	2002	2001
Plan assets				
Fair value, beginning of year	$ 152,609	$ 142,269	$ –	$ –
Actual return on plan assets	(676)	6,726	–	–
Employer contributions	996	1,204	–	–
Benefits paid	(5,263)	(4,272)	–	–
Acquisition *(note 3)*	–	6,682	–	–
Settlement	(26,015)	–	–	–
Fair value, end of year	121,651	152,609	–	–
Funded status – plan surplus (deficit)	14,311	30,799	(11,013)	(11,074)
Unamortized net transitional asset	(8,459)	(9,470)	–	–
Unrecognized net actuarial loss	14,644	3,678	–	–
Accrued benefit asset (liability)	$ 20,496	$ 25,007	$ (11,013)	$ (11,074)

The assumptions used in accounting for the Company's benefit obligations are as follows:

	Pension Benefits		Other Benefits	
	2002	2001	2002	2001
Discount rate	6.5%	7.0%	6.5%	7.0%
Expected return on plan assets	7.5%	7.5%	7.5%	7.5%
Rate of compensation increase	4.5%	4.5%	4.5%	4.5%

For measurement purposes, an 8.75% annual rate of increase in the per capita cost of covered health care benefits was assumed for 2002. The rate was assumed to decrease by 1% per annum to 5.75% in 2005 and remain at that level thereafter. Dental costs were assumed to increase at a constant 6% per year. Increasing (or decreasing) these assumptions by 1% per year would increase (or decrease) post-retirement benefits expense for the year by $2 respectively.

24. Contingent liabilities

From time to time in connection with its operations, the Company is named as a defendant in actions for damages and costs allegedly sustained by the plaintiffs. While it is not possible to estimate the outcome of the various proceedings at this time, such actions have generally been resolved with minimal expenses in excess of amounts provided for in policy liabilities and the Company does not believe that it will incur any significant additional loss or expense in connection with such actions.

25. Commitments

Future minimum payments under non-cancellable operating leases for premises and equipment having terms in excess of one year consist of: 2003 - $13,192; 2004 - $11,028; 2005 - $10,174; 2006 - $9,869; 2007 - $9,724 and thereafter - $47,523.

26. Segmented information

The Company operates in the Canadian life insurance industry and conducts its operations in three major business line divisions that cover three operating segments: Retail Protection, Asset Gathering, and Group Life & Health. Retail Protection covers individuals and includes traditional whole and term life, disability, critical illness insurance as well as universal life products. The Asset Gathering segment includes individual and group immediate and deferred annuities, institutional annuities, guaranteed savings and segregated fund investments. Group Life & Health includes group life and accident & sickness insurance.

The Retail Protection and Asset Gathering segments are managed under the Retail Division, with the exception of group immediate and deferred annuities and institutional annuities, because they share the same distribution channels and have common marketing strategies. The group immediate and deferred annuities and institutional annuities are managed within the Pensions and Group Investments Division as these products are aimed at institutional and corporate customers. The group life and accident and sickness insurance products are managed by the Group Division.

The Company's Corporate & Other segment is comprised of the Investments Division, the Corporate Division and emerging business lines. The Investments Division has responsibility for ensuring the assets supporting the policy liabilities are appropriately invested. Investment income is reported within the business segment to which the underlying invested assets are matched. The Corporate Division is responsible for the staff, facility and technology infrastructures, corporate finance, capital management, legislative and regulatory compliance and corporate governance. Emerging businesses include those operating segments that do not yet meet the quantitative criteria for separate disclosure as a reportable segment.

The following chart shows summarized operating income by reportable segment. For policy liabilities and supporting assets, also see note 9. Unusual items, income taxes and goodwill amortization are not allocated to operating segments.

2002	Retail Protection	Asset Gathering	Group Life & Health	Corporate & Others	Total
Revenue					
Premiums	$ 518,099	$ 505,416	$ 863,764	$ –	$1,887,279
Investment income	105,564	125,415	90,089	77,845	398,913
Segregated fund fees	679	111,083	–	–	111,762
Other	1,028	282	35,268	4,316	40,894
	625,370	742,196	989,121	82,161	2,438,848
Policy benefits and expenses					
Policy benefits paid and accrued	418,589	668,435	805,968	–	1,892,992
Commissions, selling and operating expenses	178,097	110,398	159,892	5,040	453,427
Transfer from segregated funds	(63)	(68,675)	–	–	(68,738)
Interest on notes payable	8,210	–	–	–	8,210
Interest on subordinated debt	–	–	–	19,874	19,874
	604,833	710,158	965,860	24,914	2,305,765
Operating income before unusual items, income taxes and goodwill amortization	$ 20,537	$ 32,038	$ 23,261	$ 57,247	$ 133,083

2001	Retail Protection	Asset Gathering	Group Life & Health	Corporate & Others	Total
Revenue					
Premiums	$ 456,070	$ 119,087	$ 780,833	$ –	$1,355,990
Investment income	101,288	108,813	89,739	91,716	391,556
Segregated fund fees	28	99,105	–	–	99,133
Other	690	600	33,704	(1,018)	33,976
	558,076	327,605	904,276	90,698	1,880,655
Policy benefits and expenses					
Policy benefits paid and accrued	285,293	189,778	734,407	–	1,209,478
Commissions, selling and operating expenses	161,760	99,634	139,808	17,532	418,734
Transfer to (from) segregated funds	(149)	17,845	–	–	17,696
Interest on notes payable	9,435	–	–	–	9,435
Interest on subordinated debt	–	–	–	15,027	15,027
	456,339	307,257	874,215	32,559	1,670,370
Operating income before unusual items, income taxes and goodwill amortization	$ 101,737	$ 20,348	$ 30,061	$ 58,139	$ 210,285

27. Supplemental cash flow information

Cash flows from investing activities

Cash flows from investing activities include the following summary transactions involving invested assets:

	2002	2001
Sales, maturities, prepayments and scheduled redemption of:		
Bonds	$ 1,409,577	$ 1,201,869
Equities	104,728	202,258
Real estate	3,414	5,539
Mortgages	232,378	312,258
Other	(1,020)	44,900
	$ 1,749,077	$ 1,766,824

	2002	2001
Purchase/issue of:		
Bonds	$ (1,811,901)	$ (1,243,035)
Equities	(173,775)	(417,707)
Real estate	(15,581)	(1,224)
Mortgages	(471,133)	(506,659)
Other	(54,249)	(11,202)
	$ (2,526,639)	$ (2,179,827)

Cash and cash equivalents definition

	2002	2001
Outstanding cheques	$ (25,107)	$ (14,770)
Term deposits with original maturities of 90 days or less, at interest rates of 1.27% to 3.11%(2001 - 1.86% to 5.63%)	245,297	102,772
	$ 220,190	$ 88,002

Other supplementary cash information.

	2002	2001
Cash paid for:		
Interest	$ 34,324	$ 39,675
Dividends on redeemable preferred shares	7,148	7,620
Income taxes	22,069	7,150
	$ 63,541	$ 54,445
Cash dividends and interest received	$ 418,203	$ 361,554

28. Subsequent Event

On January 13, 2003, the Company entered into an agreement to recapture significant portions of its Group Life, Accidental Death and Dismemberment and Long Term Disability reinsurance. This agreement was settled on January 17, 2003 for total proceeds of $270.4 million, including the receipt of $181.4 million of cash and invested assets and the concurrent settlement of a note payable obligation *(see note 11)* of $89.0 million.

29. Comparative figures

Certain of the comparative figures have been reclassified to conform to the presentation adopted in the current year.

Overview of Corporate Governance Practices

GOOD CORPORATE governance is the foundation of a financially solid company and underpins the financial well-being of all Maritime Life stakeholders: policyholders, shareholders, distribution partners and employees. The corporate governance framework within which Maritime Life operates has allowed it to meet the evolving expectations of our stakeholders.

Mandate of the Board of Directors

The Board of Directors is responsible for the stewardship of Maritime Life. The Board expects management to operate the Company in a financially sound and ethical manner, to foster growth and profit, and to provide clear and concise information on the operations and future direction of the Company.

As part of its stewardship activities, the Board oversees the development by management of:

- overall corporate strategy that results in meaningful policyholder and shareholder value;
- prudent risk management policies and practices, including the integrity of the internal control and management information systems;
- appropriate succession planning for senior executive roles;
- effective regulatory compliance procedures and adherence to the laws and regulations governing the Company; and
- fair, transparent and timely reporting of the financial results of the Company.

Composition of the Board of Directors

The number of directors of the Company can range from 12 to 20, At December 31, 2002, there were 17 directors, a majority of whom are unrelated. All directors, except the President & Chief Executive Officer, are independent of management. Maritime Life's common shares are ultimately owned by John Hancock Financial Services, Inc., ("John Hancock") through a Canadian holding company. During 2002, three senior officers of John Hancock were actively involved on the Company's Board and provided direct shareholder feedback. A further five directors are elected annually to represent shareholder interests. Nine directors are elected annually to represent the interests of participating policyholders. The Chairman of the Board is a former officer of the Company who is now separate from management and has been since 1995.

Maritime Life looks for breadth of expertise in recruiting new directors and seeks a diversity of professional backgrounds and national representation.

Corporate Structure

Principal Subsidiaries	*Address*	*Beneficial Ownership*	*Book Value of Capital Stock ($000's)*
Landex Properties Limited	Vancouver, B.C.	100%	$ 2,476
Eclipse Claims Services Inc.	Toronto, ON	25%	-
Churchill Office Park Limited	Toronto, ON	45%	-
PVS Preferred Vision Services Inc.	Toronto, ON	20%	145
Financial Life Assurance Company of Canada	Toronto, ON	100%	0
Equinox Financial Group Inc.	Toronto, ON	8%	1,100

The Board, including its committees, met five times in 2002, both with and without management present. With the exception of the Executive Committee, committees of the Board are composed of a majority of directors unrelated to the common shareholder or management of the Company.

Committees of the Board

The Board is assisted in fulfilling its responsibilities through the work of six committees, all of which are minuted and report to the full Board.

The Executive Committee, comprised of the Chairman of the Board, the President & Chief Executive Officer and representatives of the common shareholder, acts on behalf of the Board in connection with Company business between meetings of the Board of Directors.

The Investment Committee oversees the investing and lending of the funds of the Company in accordance with prudent investment policies and the provisions of the Insurance Companies Act of Canada.

The Conduct Review and Corporate Governance Committee monitors and sets policy relating to self-dealing and conflicts of interest, oversees the Company's compliance function and corporate governance practices and advises management generally on matters of corporate conduct.

The Customer Issues Committee oversees activities relating to the Company's customers, including the monitoring of customer satisfaction levels, approval of the dividend scale for participating policies, as well as performance of and compliance with the Company's risk management policies relating to product design and pricing, and underwriting and liability management.

The Audit Committee, comprised of a majority of unaffiliated directors, reviews the Company's internal controls, reviews accounting policies, engages independent external auditors and reviews the annual external audit plan and non-audit services, if any, reviews the internal audit plan annually and reviews the financial reporting and disclosure practices for both the general fund of the Company and its segregated funds. The Audit Committee's charter is reviewed annually to ensure that it reflects evolving best practices for Audit Committees.

The Human Resources Committee approves the Company's compensation plans and philosophy, recommends the appointment of the president and senior officers, oversees the Company's succession planning, reviews and approves principles for the recruitment, hiring, training and evaluation of employees and advises management generally on human resource related issues.

Dividend Scale

Dividend scales for participating insurance policies are declared on an annual basis and distributed according to the contract. The amount of surplus available for distribution is influenced by trends in earnings and experience, by dividend guarantees and by the need to maintain the long-term vitality of the participating fund. Maritime Life uses the contribution principle to allocate divisible surplus to individual policies in proportion to their contribution to earnings. The allocation process strives to ensure reasonable equity among different classes and generations of participating policies as well as equity among individual policies within each class. The determination of dividends complies with regulatory and professional standards.

Management and Directors

Senior Management Team

William A. Black
President and Chief Executive Officer

Melvin D. Bartlett
Senior Vice President, Retail Marketing

Murray Coolican
Senior Vice President, Corporate Resources

Joanne M. Keigan
Senior Vice President, Retail Operations

Josephine E. Marks
Senior Vice President, Pensions & Group Investments

Robert M. Nicholas
Senior Vice President, Group Insurance

Philip J. Pothier
Senior Vice President and Chief Financial Officer

Cecil B. Smith
Senior Vice President and Chief Information Officer

Peter A. Stuart
Senior Vice President and Chief Investment Officer

Front row from left to right: ***Mel Bartlett, Phil Pothier, Joanne Keigan, Peter Stuart, Josephine Marks***

Back row from left to right: ***Bill Black, Bob Nicholas, Cecil Smith, Murray Coolican***

Our Vision

Our vision is to be a leading provider of financial security products, offering exceptional customer service from satisfied employees, resulting in superior profitability and growth.

Board of Directors

William A. Black (12/12)
Halifax, Nova Scotia 1, 4, 5
President and Chief Executive Officer
The Maritime Life
Assurance Company

Ronald B. Coleman (10/15)
Calgary, Alberta 2, 5
President
Dominion Equity Resource Fund Inc.

J. Dickson Crawford (21/21)
Mahone Bay, Nova Scotia 1, 3, 4, 6
Chairman of the Board
The Maritime Life
Assurance Company

Mark W. (Sam) Davis (13/14)
Boston, Massachusetts 2, 5
Vice President
Real Estate Investment Group
John Hancock Financial Services, Inc.

John R. D' Eathe (10/10)
West Vancouver, British Columbia 5
President
Freehold Development Canada Ltd.

Robert P. Dexter, QC (15/15)
Halifax, Nova Scotia 2, 5
Chairman and Chief Executive
Officer
Maritime Travel

MGen. (Ret'd) M. Scott Eichel (14/14)
Victoria, British Columbia 3, 4
President
Eichel Aviation Services Inc.

Ruth M. Grant (9/15)
Toronto, Ontario 2, 4
President
Craigellachie Holdings Ltd.

Lawrence J. Hayes, QC (19/19)
Halifax, Nova Scotia 3, 4, 6
McInnes Cooper

Jean C. Lavoie (15/15)
Montreal, Quebec 2, 4
Business Consultant

Douglas G. MacKenzie (11/14)
Oakville, Ontario 3, 5
DMCS Ltd.

Robert J. Mair, QC (14/15)
Vancouver, British Columbia 2, 4
Partner
Lawson Lundell

Thomas E. Moloney (17/17)
Boston, Massachusetts 1, 5, 6
Senior Executive Vice President and
Chief Financial Officer
John Hancock Financial Services, Inc.

Jocelyne Pelchat (19/19)
Town of Mount Royal, Quebec 3, 4, 6
President and CEO
Entreprises Pelchat Moïse Inc.

Anna Porter, OC (7/10)
Toronto, Ontario 5
Publisher and CEO
Key Porter Books

Robert R. Reitano (6/10)
Boston, Massachusetts 5
Senior Vice President and Chief
Investment Strategist
Investment Strategy Group
John Hancock Financial Services, Inc.

Dr. Thomas D. Traves (13/14)
Halifax, Nova Scotia 3, 4
President and Vice-Chancellor
Dalhousie University

Honorary Directors for 2002

Dr. D. Andrew Eisenhauer
Lunenburg, Nova Scotia

Fraser M. Fell, QC
Toronto, Ontario

Dr. Reva D. Gerstein, CC, O.Ont.
Toronto, Ontario

Mr. John W. Lindsay, Sr.
Dartmouth, Nova Scotia

The bracketed numbers following each name indicate the total number of board and committee meetings which the director attended, followed by the number they were eligible to attend in the 12 months ended December 31, 2002. The numbers following the director's location indicate the board committee memberships.

1. Executive Committee
2. Audit Committee
3. Conduct Review and Corporate Governance Committee
4. Customer Issues Committee
5. Investment Committee
6. Human Resources Committee

Head office

7 Maritime Place
P.O. Box 1030
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(902) 453-4300

Annual General Meeting

April 2, 2003, 11:00 a.m. (AST)
7 Maritime Place
Halifax, Nova Scotia

Stock Symbols

Series A, First Preferred Shares:
MMF.PR.A
Series 1, Second Preferred Shares:
MMF.PR.B
Series 3, Second Preferred Shares:
MMF.PR.C

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